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Internal Revenue Code Section 461(l)(3)(A)

General rule for taxable year of deduction

(a) General rule.

The amount of any deduction or credit allowed by this subtitle shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income.

(b) Special rule in case of death.

In the case of the death of a taxpayer whose taxable income is computed under an accrual method of accounting, any amount accrued as a deduction or credit only by reason of the death of the taxpayer shall not be allowed in computing taxable income for the period in which falls the date of the taxpayer's death.

(c) Accrual of real property taxes.

(1) In general.

If the taxable income is computed under an accrual method of accounting, then, at the election of the taxpayer, any real property tax which is related to a definite period of time shall be accrued ratably over that period.

(2) When election may be made.

(A) Without consent. A taxpayer may, without the consent of the Secretary, make an election under this subsection for his first taxable year in which he incurs real property taxes. Such an election shall be made not later than the time prescribed by law for filing the return for such year (including extensions thereof).

(B) With consent. A taxpayer may, with the consent of the Secretary, make an election under this subsection at any time.

(d) Limitation on acceleration of accrual of taxes.

(1) General rule.

In the case of a taxpayer whose taxable income is computed under an accrual method of accounting, to the extent that the time for accruing taxes is earlier than it would be but for any action of any taxing jurisdiction taken after December 31, 1960, then, under regulations prescribed by the Secretary, such taxes shall be treated as accruing at the time they would have accrued but for such action by such taxing jurisdiction.

(2) Limitation.

Under regulations prescribed by the Secretary, paragraph (1) shall be inapplicable to any item of tax to the extent that its application would (but for this paragraph) prevent all persons (including successors in interest) from ever taking such item into account.

(e) Dividends or interest paid on certain deposits or withdrawable accounts.

Except as provided in regulations prescribed by the Secretary, amounts paid to, or credited to the accounts of, depositors or holders of accounts as dividends or interest on their deposits or withdrawable accounts (if such amounts paid or credited are withdrawable on demand subject only to customary notice to withdraw) by a mutual savings bank not having capital stock represented by shares, a domestic building and loan association, or a cooperative bank shall not be allowed as a deduction for the taxable year to the extent such amounts are paid or credited for periods representing more than 12 months. Any such amount not allowed as a deduction as the result of the application of the preceding sentence shall be allowed as a deduction for such other taxable year as the Secretary determines to be consistent with the preceding sentence.

(f) Contested liabilities.

If-

(1) the taxpayer contests an asserted liability,

(2) the taxpayer transfers money or other property to provide for the satisfaction of the asserted liability,

(3) the contest with respect to the asserted liability exists after the time of the transfer, and

(4) but for the fact that the asserted liability is contested, a deduction would be allowed for the taxable year of the transfer (or for an earlier taxable year) determined after application of subsection (h) ,

then the deduction shall be allowed for the taxable year of the transfer. This subsection shall not apply in respect of the deduction for income, war profits, and excess profits taxes imposed by the authority of any foreign country or possession of the United States.

(g) Prepaid interest.

(1) In general.

If the taxable income of the taxpayer is computed under the cash receipts and disbursements method of accounting, interest paid by the taxpayer which, under regulations prescribed by the Secretary, is properly allocable to any period-

(A) with respect to which the interest represents a charge for the use or forbearance of money, and

(B) which is after the close of the taxable year in which paid,

shall be charged to capital account and shall be treated as paid in the period to which so allocable.

(2) Exception.

This subsection shall not apply to points paid in respect of any indebtedness incurred in connection with the purchase or improvement of, and secured by, the principal residence of the taxpayer to the extent that, under regulations prescribed by the Secretary, such payment of points is an established business practice in the area in which such indebtedness is incurred, and the amount of such payment does not exceed the amount generally charged in such area.

(h) Certain liabilities not incurred before economic performance.

(1) In general.

For purposes of this title, in determining whether an amount has been incurred with respect to any item during any taxable year, the all events test shall not be treated as met any earlier than when economic performance with respect to such item occurs.

(2) Time when economic performance occurs.

Except as provided in regulations prescribed by the Secretary, the time when economic performance occurs shall be determined under the following principles:

(A) Services and property provided to the taxpayer. If the liability of the taxpayer arises out of-

(i) the providing of services to the taxpayer by another person, economic performance occurs as such person provides such services,

(ii) the providing of property to the taxpayer by another person, economic performance occurs as the person provides such property, or

(iii) the use of property by the taxpayer, economic performance occurs as the taxpayer uses such property.

(B) Services and property provided by the taxpayer. If the liability of the taxpayer requires the taxpayer to provide property or services, economic performance occurs as the taxpayer provides such property or services.

(C) Workers compensation and tort liabilities of the taxpayer. If the liability of the taxpayer requires a payment to another person and-

(i) arises under any workers compensation act, or

(ii) arises out of any tort,

economic performance occurs as the payments to such person are made.

Subparagraphs (A) and (B) shall not apply to any liability described in the preceding sentence.

(D) Other items. In the case of any other liability of the taxpayer, economic performance occurs at the time determined under regulations prescribed by the Secretary.

(3) Exception for certain recurring items.

(A) In general. Notwithstanding paragraph (1) an item shall be treated as incurred during any taxable year if-

(i) the all events test with respect to such item is met during such taxable year (determined without regard to paragraph (1)),

(ii) economic performance with respect to such item occurs within the shorter of-

(I) a reasonable period after the close of such taxable year, or

(II) 8½ months after the close of such taxable year,

(iii) such item is recurring in nature and the taxpayer consistently treats items of such kind as incurred in the taxable year in which the requirements of clause (i) are met, and

(iv) either-

(I) such item is not a material item, or

(II) the accrual of such item in the taxable year in which the requirements of clause (i) are met results in a more proper match against income than accruing such item in the taxable year in which economic performance occurs.

(B) Financial statements considered under subparagraph (A)(iv) . In making a determination under subparagraph (A)(iv) , the treatment of such item on financial statements shall be taken into account.

(C) Paragraph not to apply to workers compensation and tort liabilities. This paragraph shall not apply to any item described in subparagraph (C) of paragraph (2) .

(4) All events test.

For purposes of this subsection , the all events test is met with respect to any item if all events have occurred which determine the fact of liability and the amount of such liability can be determined with reasonable accuracy.

(5) Subsection not to apply to certain items.

This subsection shall not apply to any item for which a deduction is allowable under a provision of this title which specifically provides for a deduction for a reserve for estimated expenses.

(i) Special rules for tax shelters.

(1) Recurring item exception not to apply.

In the case of a tax shelter, economic performance shall be determined without regard to paragraph (3) of subsection (h) .

(2) Special rule for spudding of oil or gas wells.

(A) In general. In the case of a tax shelter, economic performance with respect to amounts paid during the taxable year for drilling an oil or gas well shall be treated as having occurred within a taxable year if drilling of the well commences before the close of the 90th day after the close of the taxable year.

(B) Deduction limited to cash basis.

(i) Tax shelter partnerships. In the case of a tax shelter which is a partnership, in applying section 704(d) to a deduction or loss for any taxable year attributable to an item which is deductible by reason of subparagraph (A) , the term "cash basis" shall be substituted for the term "adjusted basis".

(ii) Other tax shelters. Under regulations prescribed by the Secretary, in the case of a tax shelter other than a partnership, the aggregate amount of the deductions allowable by reason of subparagraph (A) for any taxable year shall be limited in a manner similar to the limitation under clause (i) .

(C) Cash basis defined. For purposes of subparagraph (B) , a partner's cash basis in a partnership shall be equal to the adjusted basis of such partner's interest in the partnership, determined without regard to-

(i) any liability of the partnership, and

(ii) any amount borrowed by the partner with respect to such partnership which-

(I) was arranged by the partnership or by any person who participated in the organization, sale, or management of the partnership (or any person related to such person within the meaning of section 465(b)(3)(C)), or

(II) was secured by any asset of the partnership.

(3) Tax shelter defined.

For purposes of this subsection , the term "tax shelter" means-

(A) any enterprise (other than a C corporation) if at any time interests in such enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having the authority to regulate the offering of securities for sale,

(B) any syndicate (within the meaning of section 1256(e)(3)(B)), and

(C) any tax shelter (as defined in section 6662(d)(2)(C)(ii)).

(4) Special rules for farming.

In the case of the trade or business of farming (as defined in section 464(e)), in determining whether an entity is a tax shelter, the definition of farming syndicate in subsection (k) shall be substituted for subparagraphs (A) and (B) of paragraph (3) .

(5) Economic performance.

For purposes of this subsection , the term "economic performance" has the meaning given such term by subsection (h) .

(j) Limitation on excess farm losses of certain taxpayers.

(1) Limitation.

If a taxpayer other than a C corporation receives any applicable subsidy for any taxable year, any excess farm loss of the taxpayer for the taxable year shall not be allowed.

(2) Disallowed loss carried to next taxable year.

Any loss which is disallowed under paragraph (1) shall be treated as a deduction of the taxpayer attributable to farming businesses in the next taxable year.

(3) Applicable subsidy.

For purposes of this subsection, the term "applicable subsidy" means-

(A) any direct or counter-cyclical payment under title I of the Food, Conservation, and Energy Act of 2008, or any payment elected to be received in lieu of any such payment, or

(B) any Commodity Credit Corporation loan.

(4) Excess farm loss.

For purposes of this subsection -

(A) In general. The term "excess farm loss" means the excess of-

(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to farming businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1)), over

(ii) the sum of-

(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such farming businesses, plus

(II) the threshold amount for the taxable year.

(B) Threshold amount.

(i) In general. The term "threshold amount" means, with respect to any taxable year, the greater of-

(I) \$300,000 (\$150,000 in the case of married individuals filing separately), or

(II) the excess (if any) of the aggregate amounts described in subparagraph (A)(ii)(I) for the 5-consecutive taxable year period preceding the taxable year over the aggregate amounts described in subparagraph (A)(i) for such period.

(ii) Special rules for determining aggregate amounts. For purposes of clause (i)(II) -

(I) notwithstanding the disregard in subparagraph (A)(i) of any disallowance under paragraph (1) , in the case of any loss which is carried forward under paragraph (2) from any taxable year, such loss (or any portion thereof) shall be taken into account for the first taxable year in which a deduction for such loss (or portion) is not disallowed by reason of this subsection , and

(II) the Secretary shall prescribe rules for the computation of the aggregate amounts described in such clause in cases where the filing status of the taxpayer is not the same for the taxable year and each of the taxable years in the period described in such clause.

(C) Farming business.

(i) In general. The term "farming business" has the meaning given such term in section 263A(e)(4) .

(ii) Certain trades and businesses included. If, without regard to this clause , a taxpayer is engaged in a farming business with respect to any agricultural or horticultural commodity-

(I) the term "farming business" shall include any trade or business of the taxpayer of the processing of such commodity (without regard to whether the processing is incidental to the growing, raising, or harvesting of such commodity), and

(II) if the taxpayer is a member of a cooperative to which subchapter T applies, any trade or business of the cooperative described in subclause (I) shall be treated as the trade or business of the taxpayer.

(D) Certain losses disregarded. For purposes of subparagraph (A)(i) , there shall not be taken into account any deduction for any loss arising by reason of fire, storm, or other casualty, or by reason of disease or drought, involving any farming business.

(5) Application of subsection in case of partnerships and S corporations.

In the case of a partnership or S corporation-

(A) this subsection shall be applied at the partner or shareholder level, and

(B) each partner's or shareholder's proportionate share of the items of income, gain, or deduction of the partnership or S corporation for any taxable year from farming businesses attributable to the partnership or S corporation, and of any applicable subsidies received by the partnership or S corporation during the taxable year, shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

The Secretary may provide rules for the application of this paragraph to any other pass-thru entity to the extent necessary to carry out the provisions of this subsection .

(6) Additional reporting.

The Secretary may prescribe such additional reporting requirements as the Secretary determines appropriate to carry out the purposes of this subsection.

(7) Coordination with section 469.

This subsection shall be applied before the application of section 469 .

(k) Farming syndicate defined.

(1) In general.

For purposes of subsection (i)(4) , the term "farming syndicate" means-

(A) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if at any time interests in such partnership or enterprise have been offered for sale in any offering

required to be registered with any Federal or State agency having authority to regulate the offering of securities for sale, or

(B) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if more than 35 percent of the losses during any period are allocable to limited partners or limited entrepreneurs.

(2) Holdings attributable to active management.

For purposes of paragraph (1)(B) , the following shall be treated as an interest which is not held by a limited partner or a limited entrepreneur:

(A) in the case of any individual who has actively participated (for a period of not less than 5 years) in the management of any trade or business of farming, any interest in a partnership or other enterprise which is attributable to such active participation,

(B) in the case of any individual whose principal residence is on a farm, any partnership or other enterprise engaged in the trade or business of farming such farm,

(C) in the case of any individual who is actively participating in the management of any trade or business of farming or who is an individual who is described in subparagraph (A) or (B) , any participation in the further processing of livestock which was raised in such trade or business (or in the trade or business referred to in subparagraph (A) or (B)),

(D) in the case of an individual whose principal business activity involves active participation in the management of a trade or business of farming, any interest in any other trade or business of farming, and

(E) any interest held by a member of the family (or a spouse of any such member) of a grandparent of an individual described in subparagraph (A) , (B) , (C) , or (D) if the interest in the partnership or the enterprise is attributable to the active participation of the individual described in subparagraph (A) , (B) , (C) , or (D) .

For purposes of subparagraph (A) , where one farm is substituted for or added to another farm, both farms shall be treated as one farm. For purposes of subparagraph (E) , the term "family" has the meaning given to such term by section 267(c)(4) .

(3) Farming.

For purposes of this subsection , the term "farming" has the meaning given to such term by section 464(e) .

(4) limited entrepreneur.

For purposes of this subsection, the term "limited entrepreneur" means a person who-

(A) has an interest in an enterprise other than as a limited partner, and

(B) does not actively participate in the management of such enterprise.

(l) Limitation on excess business losses of noncorporate taxpayers.

(1) Limitation.

In the case of a taxpayer other than a corporation-

(A) for any taxable year beginning after December 31, 2017, and before January 1, 2027, subsection (j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and

(B) for any taxable year beginning after December 31, 2020, and before January 1, 2027, any excess business loss of the taxpayer for the taxable year shall not be allowed.

Note: Section 461(l)(1), below, shall apply to tax years beginning after Dec. 31, 2026. See above for Section 461(l)(1), as it applies to tax years beginning before Jan. 1, 2027.

(1) Limitation.

In the case of a taxpayer other than a corporation-

(A) for any taxable year beginning after December 31, 2017, and before January 1, 2029, subsection (j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and

(B) for any taxable year beginning after December 31, 2020, and before January 1, 2029, any excess business loss of the taxpayer for the taxable year shall not be allowed.

(2) Disallowed loss carryover.

Any loss which is disallowed under paragraph (1) shall be treated as a net operating loss for the taxable year for purposes of determining any net operating loss carryover under section 172(b) for subsequent taxable years.

(3) Excess business loss.

For purposes of this subsection-

(A) In general. The term "excess business loss" means the excess (if any) of-

(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to trades or businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1) and without regard to any deduction allowable under section 172 or 199A), over

(ii) the sum of-

(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such trades or businesses, plus

(II) \$250,000 (200 percent of such amount in the case of a joint return).

Such excess shall be determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee.



(B) Treatment of capital gains and losses.

(i) Losses. Deductions for losses from sales or exchanges of capital assets shall not be taken into account under subparagraph (A)(i).

(ii) Gains. The amount of gains from sales or exchanges of capital assets taken into account under subparagraph (A)(ii) shall not exceed the lesser of-

(I) the capital gain net income determined by taking into account only gains and losses attributable to a trade or business, or

(II) the capital gain net income.

(C) Adjustment for inflation. In the case of any taxable year beginning after December 31, 2018, the \$250,000 amount in subparagraph (A)(ii)(II) shall be increased by an amount equal to-

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting "2017" for "2016" in subparagraph (A)(ii) thereof.

If any amount as increased under the preceding sentence is not a multiple of \$1,000, such amount shall be rounded to the nearest multiple of \$1,000.

(4) Application of subsection in case of partnerships and S corporations.

In the case of a partnership or S corporation-

(A) this subsection shall be applied at the partner or shareholder level, and

(B) each partner's or shareholder's allocable share of the items of income, gain, deduction, or loss of the partnership or S corporation for any taxable year from trades or businesses attributable to the partnership or S corporation shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

For purposes of this paragraph, in the case of an S corporation, an allocable share shall be the shareholder's pro rata share of an item.

(5) Additional reporting.

The Secretary shall prescribe such additional reporting requirements as the Secretary determines necessary to carry out the purposes of this subsection .

(6) Coordination with section 469.

This subsection shall be applied after the application of section 469 .