

Treasury Regulations Under Code Section 482

Allocation of Income and Deductions among Taxpayers

Reg. § 1.482-2 (2009)

Determination of taxable income in specific situations

(a) *Loans or advances.*—

(1) *Interest on bona fide indebtedness.*

(i) *In general.* Where one member of a group of controlled entities makes a loan or advance directly or indirectly to, or otherwise becomes a creditor of, another member of such group and either charges no interest, or charges interest at a rate which is not equal to an arm's length rate of interest (as defined in paragraph (a)(2) of this section) with respect to such loan or advance, the district director may make appropriate allocations to reflect an arm's length rate of interest for the use of such loan or advance.

(ii) *Application of paragraph (a) of this section.*

(A) *Interest on bona fide indebtedness.* Paragraph (a) of this section applies only to determine the appropriateness of the rate of interest charged on the principal amount of a bona fide indebtedness between members of a group of controlled entities, including—

(1) Loans or advances of money or other consideration (whether or not evidenced by a written instrument); and

(2) Indebtedness arising in the ordinary course of business from sales, leases, or the rendition of services by or between members of the group, or any other similar extension of credit.

(B) *Alleged indebtedness.* This paragraph (a) does not apply to so much of an alleged indebtedness which is not in fact a bona fide indebtedness, even if the stated rate of interest thereon would be within the safe haven rates prescribed in paragraph (a)(2)(iii) of this section. For example, paragraph (a) of this section does not apply to payments with respect to all or a portion of such alleged indebtedness where in fact all or a portion of an alleged indebtedness is a contribution to the capital of a corporation or a distribution by a corporation with respect to its shares. Similarly, this paragraph (a) does not apply to payments with respect to an alleged purchase-money debt instrument given in consideration for an alleged sale of property between two controlled entities where in fact the transaction constitutes a lease of the property. Payments made with respect to alleged indebtedness (including alleged stated interest thereon) shall be treated according to their substance. See section 1.482-2(a)(3)(i).

(iii) *Period for which interest shall be charged.*

(A) *General rule.* This paragraph (a)(1)(iii) is effective for indebtedness arising after June 30, 1988. See section 1.482-2(a)(3)(26 CFR Part 1 edition revised as of April 1, 1988) for indebtedness arising before July 1, 1988. Except as otherwise provided in paragraphs (a)(1)(iii)(B) through (E) of this section, the period for which interest shall be charged with respect to a bona fide indebtedness between controlled entities begins on the day after the day the indebtedness arises and ends on the day the indebtedness is satisfied (whether by payment, offset, cancellation, or otherwise). Paragraphs (a)(1)(iii)(B) through (E) of this section provide certain alternative periods during which interest is not required to be charged on certain indebtedness. These exceptions apply only to indebtedness described in paragraph (a)(1)(ii)(A)(2) of this section (relating to indebtedness incurred in the ordinary course of business from sales, services, etc., between members of the group) and not evidenced by a written instrument requiring the payment of interest. Such amounts are hereinafter referred to as intercompany trade receivables. The period for which interest is not required to be charged on intercompany trade receivables under this paragraph (a)(1)(iii) is called the interest-free period. In general, an intercompany

trade receivable arises at the time economic performance occurs (within the meaning of section 461(h) and the regulations thereunder) with respect to the underlying transaction between controlled entities. For purposes of this paragraph (a)(1)(iii), the term United States includes any possession of the United States, and the term foreign country excludes any possession of the United States.

(B) *Exception for certain intercompany transactions in the ordinary course of business.*

Interest is not required to be charged on an intercompany trade receivable until the first day of the third calendar month following the month in which the intercompany trade receivable arises.

(C) *Exception for trade or business of debtor member located outside the United States.* In the case of an intercompany trade receivable arising from a transaction in the ordinary course of a trade or business which is actively conducted outside the United States by the debtor member, interest is not required to be charged until the first day of the fourth calendar month following the month in which such intercompany trade receivable arises.

(D) *Exception for regular trade practice of creditor member or others in creditor's industry.* If the creditor member or unrelated persons in the creditor member's industry, as a regular trade practice, allow unrelated parties a longer period without charging interest than that described in paragraph (a)(1)(iii)(B) or (C) of this section (whichever is applicable) with respect to transactions which are similar to transactions that give rise to intercompany trade receivables, such longer interest-free period shall be allowed with respect to a comparable amount of intercompany trade receivables.

(E) *Exception for property purchased for resale in a foreign country.*

(1) *General rule.* If in the ordinary course of business one member of the group (related purchaser) purchases property from another member of the group (related seller) for resale to unrelated persons located in a particular foreign country, the related purchaser and the related seller may use as the interest-free period for the intercompany trade receivables arising during the related seller's taxable year from the purchase of such property within the same product group an interest-free period equal the sum of—

(i) The number of days in the related purchaser's average collection period (as determined under paragraph (a)(1)(iii)(E)(2) of this section) for sales of property within the same product group sold in the ordinary course of business to unrelated persons located in the same foreign country; plus

(ii) Ten (10) calendar days.

(2) *Interest-free period.* The interest-free period under this paragraph (a)(1)(iii)(E), however, shall in no event exceed 183 days. The related purchaser does not have to conduct business outside the United States in order to be eligible to use the interest-free period of this paragraph (a)(1)(iii)(E). The interest-free period under this paragraph (a)(1)(iii)(E) shall not apply to intercompany trade receivables attributable to property which is manufactured, produced, or constructed (within the meaning of section 1.954-3(a)(4)) by the related purchaser. For purposes of this paragraph (a)(1)(iii)(E) a product group includes all products within the same three-digit Standard Industrial Classification (sic) Code (as prepared by the Statistical Policy Division of the Office of Management and Budget, Executive Office of the President.)

(3) *Average collection period.* An average collection period for purposes of this paragraph (a)(1)(iii)(E) is determined as follows—

(i) *Step 1.* Determine total sales (less returns and allowances) by the related purchaser in the product group to unrelated persons located in the same foreign country during the related purchaser's last taxable year ending on or before the first day of the related seller's taxable year in which the intercompany trade receivable arises.

(ii) *Step 2.* Determine the related purchaser's average month-end accounts receivable balance with respect to sales described in paragraph (a)(1)(iii)(E)(2)(i) of this section for the related purchaser's last taxable year ending on or before the first day of the related seller's taxable year in which the intercompany trade receivable arises.

(iii) *Step 3.* Compute a receivables turnover rate by dividing the total sales amount described in paragraph (a)(1)(iii)(E)(2)(i) of this section by the average receivables balance described in paragraph (a)(1)(iii)(E)(2)(ii) of this section.

(iv) *Step 4.* Divide the receivables turnover rate determined under paragraph (a)(1)(iii)(E)(2)(iii) of this section into 365, and round the result to the nearest whole number to determine the number of days in the average collection period.

(v) *Other considerations.* If the related purchaser makes sales in more than one foreign country, or sells property in more than one product group in any foreign country, separate computations of an average collection period, by product group within each country, are required. If the related purchaser resells fungible property in more than one foreign country and the intercompany trade receivables arising from the related party purchase of such fungible property cannot reasonably be identified with resales in particular foreign countries, then solely for the purpose of assigning an interest-free period to such intercompany trade receivables under this paragraph (a)(1)(iii)(E), an amount of each such intercompany trade receivable shall be treated as allocable to a particular foreign country in the same proportion that the related purchaser's sales of such fungible property in such foreign country during the period described in paragraph (a)(1)(iii)(E)(2)(i) of this section bears to the related purchaser's sales of all such fungible property in all such foreign countries during such period. An interest-free period under this paragraph (a)(1)(iii)(E) shall not apply to any intercompany trade receivables arising in a taxable year of the related seller if the related purchaser made no sales described in paragraph (a)(1)(iii)(E)(2)(i) of this section from which the appropriate interest-free period may be determined.

(4) *Illustration.* The interest-free period provided under paragraph (a)(1)(iii)(E) of this section may be illustrated by the following example:

Example—(i) Facts. X and Y use the calendar year as the taxable year and are members of the same group of controlled entities within the meaning of section 482. For Y's 1988 calendar taxable year X and Y intend to use the interest-free period determined under this paragraph (a)(1)(iii)(E) for intercompany trade receivables attributable to X's purchases of certain products from Y for resale by X in the ordinary course of business to unrelated persons in country Z. For its 1987 calendar taxable year all of X's sales in country Z were of products within a single product group based upon a three-digit SIC code, were not manufactured, produced, or constructed (within the meaning of section 1.954-3(a)(4)) by X, and were sold in the ordinary course of X's trade or business to unrelated persons located only in country Z. These sales and the month-end accounts receivable balances (for such sales and for such sales uncollected from prior months) are as follows:

Month	Sales	Accounts Receivable
January 1987	\$ 500,000	\$ 2,835,850
February	600,000	2,840,300
March	450,000	2,850,670
April	550,000	2,825,700
May	650,000	2,809,360
June	525,000	2,803,200
July	400,000	2,825,850
August	425,000	2,796,240

September	475,000	2,839,390
October	525,000	2,650,550
November	450,000	2,775,450
December 1987	650,000	2,812,600
TOTALS	\$6,200,000	\$33,665,160

(ii) *Average collection period.* X's total sales within the same product group to unrelated persons within country Z for the period are \$6,200,000. The average receivables balance for the period is \$2,805,430 (\$33,665,160/12). The average collection period in whole days is determined as follows:

$$\begin{array}{r} \text{Receivables} \\ \text{Turnover Rate} = \end{array} \begin{array}{r} \$6,200,000 \\ \frac{\quad}{\$2,805,430} = 2.21 \end{array}$$

$$\text{Average Collection Period} = 365$$

$$\frac{\quad}{2.21} = 165.16 \text{ days, rounded to the nearest whole day} = 165 \text{ days.}$$

$$\text{Collection Period} = 2.21$$

(iii) *Interest-free period.* Accordingly, for intercompany trade receivables incurred by X during Y's 1988 calendar taxable year attributable to the purchase of property from Y for resale to unrelated persons located in country Z and included in the product group, X may use an interest-free period of 175 days (165 days in the average collection period plus 10 days, but not in excess of a maximum of 183 days). All other intercompany trade receivables incurred by X are subject to the interest-free periods described in paragraphs (a)(1)(iii)(B), (C), or (D), whichever are applicable. If X makes sales in other foreign countries in addition to country Z or makes sales of property in more than one product group in any foreign country, separate computations of X's average collection period, by product group within each country, are required in order for X and Y to determine an interest-free period for such product groups in such foreign countries under this paragraph (a)(1)(iii)(E).

(iv) *Payment; book entries.*

(A) Except as otherwise provided in this paragraph (a)(1)(iv), in determining the period of time for which an amount owed by one member of the group to another member is outstanding, payments or other credits to an account are considered to be applied against the earliest amount outstanding, that is, payments or credits are applied against amounts in a first-in, first-out (FIFO) order. Thus, tracing payments to individual intercompany trade receivables is generally not required in order to determine whether a particular intercompany trade receivable has been paid within the applicable interest-free period determined under paragraph (a)(1)(iii) of this section. The application of this paragraph (a)(1)(iv)(A) may be illustrated by the following example:

Example (i) FACTS. X and Y are members of a group of controlled entities within the meaning of section 482. Assume that the balance of intercompany trade receivables owed by X to Y on June 1 is \$100, and that all of the \$100 balance represents amounts incurred by X to Y during the month of May. During the month of June X incurs an additional \$200 of intercompany trade receivables to Y. Assume that on July 15, \$60 is properly credited against X's intercompany account to Y, and that \$240 is properly credited against the intercompany account on August 31. Assume that under paragraph (a)(1)(iii)(B) of this section interest must be charged on X's intercompany trade receivables to Y beginning with the first day of the third calendar month following the month the intercompany trade receivables

arise, and that no alternative interest-free period applies. Thus, the interest-free period for intercompany trade receivables incurred during the month of May ends on July 31, and the interest-free period for intercompany trade receivables incurred during the month of June ends on August 31.

(ii) *Application of payments.* Using a FIFO payment order, the aggregate payments of \$300 are applied first to the opening June balance, and then to the additional amounts incurred during the month of June. With respect to X's June opening balance of \$100, no interest is required to be accrued on \$60 of such balance paid by X on July 15, because such portion was paid within its interest-free period. Interest for 31 days, from August 1 to August 31 inclusive, is required to be accrued on the \$40 portion of the opening balance not paid until August 31. No interest is required to be accrued on the \$200 of intercompany trade receivables X incurred to Y during June because the \$240 credited on August 31, after eliminating the \$40 of indebtedness remaining from periods before June, also eliminated the \$200 incurred by X during June prior to the end of the interest-free period for that amount. The amount of interest incurred by X to Y on the \$40 amount during August creates bona fide indebtedness between controlled entities and is subject to the provisions of paragraph (a)(1)(iii)(A) of this section without regard to any of the exceptions contained in paragraphs (a)(1)(iii)(B) through (E).

(B) Notwithstanding the first-in, first-out payment application rule described in paragraph (a)(1)(iv)(A) of this section, the taxpayer may apply payments or credits against amounts owed in some other order on its books in accordance with an agreement or understanding of the related parties if the taxpayer can demonstrate that either it or others in its industry, as a regular trade practice, enter into such agreements or understandings in the case of similar balances with unrelated parties.

(2) *Arm's length interest rate.*

(i) *In general.* For purposes of section 482 and paragraph (a) of this section, an arm's length rate of interest shall be a rate of interest which was charged, or would have been charged, at the time the indebtedness arose, in independent transactions with or between unrelated parties under similar circumstances. All relevant factors shall be considered, including the principal amount and duration of the loan, the security involved, the credit standing of the borrower, and the interest rate prevailing at the situs of the lender or creditor for comparable loans between unrelated parties.

(ii) *Funds obtained at situs of borrower.* Notwithstanding the other provisions of paragraph (a)(2) of this section, if the loan or advance represents the proceeds of a loan obtained by the lender at the situs of the borrower, the arm's length rate for any taxable year shall be equal to the rate actually paid by the lender increased by an amount which reflects the costs or deductions incurred by the lender in borrowing such amounts and making such loans, unless the taxpayer establishes a more appropriate rate under the standards set forth in paragraph (a)(2)(i) of this section.

(iii) *Safe haven interest rates for certain loans and advances made after May 28, 1986.*

(A) *Applicability.*

(1) *General rule.* Except as otherwise provided in paragraph (a)(2) of this section, paragraph (a)(2)(iii)(B) applies with respect to the rate of interest charged and to the amount of interest paid or accrued in any taxable year—

(i) Under a term loan or advance between members of a group of controlled entities where (except as provided in paragraph (a)(2)(iii)(A)(2)(11) of this section) the loan or advance is entered into after May 8, 1986; and

(ii) After May 8, 1986 under a demand loan or advance between such controlled entities.

(2) *Grandfather rule for existing loans.* The safe haven rates prescribed in paragraph (a)(2)(iii)(B) of this section shall not apply, and the safe haven rates prescribed in section 1.482-2(a)(2)(iii) (26 CFR part 1 edition revised as of April 1, 1985), shall apply to—

(i) Term loans or advances made before May 9, 1986; and
(ii) Term loans or advances made before August 7, 1986, pursuant to a binding written contract entered into before May 9, 1986.

(B) *Safe haven interest rate based on applicable federal rate.* Except as otherwise provided in this paragraph (a)(2), in the case of a loan or advance between members of a group of controlled entities, an arm's length rate of interest referred to in paragraph (a)(2)(i) of this section shall be for purposes of chapter 1 of the Internal Revenue Code—

(1) The rate of interest actually charged if that rate is—

(i) Not less than 100 percent of the applicable Federal rate (lower limit);
and
(ii) Not greater than 130 percent of the applicable Federal rate (upper limit); or

(2) If either no interest is charged or if the rate of interest charged is less than the lower limit, then an arm's length rate of interest shall be equal to the lower limit, compounded semiannually; or

(3) If the rate of interest charged is greater than the upper limit, then an arm's length rate of interest shall be equal to the upper limit, compounded semiannually, unless the taxpayer establishes a more appropriate compound rate of interest under paragraph (a)(2)(i) of this section. However, if the compound rate of interest actually charged is greater than the upper limit and less than the rate determined under paragraph (a)(2)(i) of this section, or if the compound rate actually charged is less than the lower limit and greater than the rate determined under paragraph (a)(2)(i) of this section, then the compound rate actually charged shall be deemed to be an arm's length rate under paragraph (a)(2)(i). In the case of any sale-leaseback described in section 1274(e), the lower limit shall be 110 percent of the applicable Federal rate, compounded semiannually.

(C) *Applicable Federal rate.* For purposes of paragraph (a)(2)(iii)(B) of this section, the term applicable Federal rate means, in the case of a loan or advance to which this section applies and having a term of—

(1) Not over 3 years, the Federal short-term rate;

(2) Over 3 years but not over 9 years, the Federal mid-term rate; or

(3) Over 9 years, the Federal long-term rate, as determined under section 1274(d) in effect on the date such loan or advance is made. In the case of any sale or exchange between controlled entities, the lower limit shall be the lowest of the applicable Federal rates in effect for any month in the 3-calendar-month period ending with the first calendar month in which there is a binding written contract in effect for such sale or exchange (lowest 3-month rate, as defined in section 1274(d)(2)). In the case of a demand loan or advance to which this section applies, the applicable Federal rate means the Federal short-term rate determined under section 1274(d) (determined without regard to the lowest 3-month short term rate determined under section 1274(d)(2)) in effect for each day on which any amount of such loan or advance (including unpaid accrued interest determined under paragraph (a)(2) of this section) is outstanding.

(D) *Lender in business of making loans.* If the lender in a loan or advance transaction to which paragraph (a)(2) of this section applies is regularly engaged in the trade or business of making loans or advances to unrelated parties, the safe haven rates prescribed in paragraph (a)(2)(iii)(B) of this section shall not apply, and the arm's length interest rate to be used shall be determined under the standards described in paragraph (a)(2)(i) of this section, including reference to the interest rates charged in such

trade or business by the lender on loans or advances of a similar type made to unrelated parties at and about the time the loan or advance to which paragraph (a)(2) of this section applies was made.

(E) *Foreign currency loans.* The safe haven interest rates prescribed in paragraph (a)(2)(iii)(B) of this section do not apply to any loan or advance the principal or interest of which is expressed in a currency other than U.S. dollars.

(3) *Coordination with interest adjustments required under certain other code sections.* If the stated rate of interest on the stated principal amount of a loan or advance between controlled entities is subject to adjustment under section 482 and is also subject to adjustment under any other section of the Internal Revenue Code (for example, section 467, 483, 1274 or 7872), section 482 and paragraph (a) of this section may be applied to such loan or advance in addition to such other Internal Revenue Code section. After the enactment of the Tax Reform Act of 1964, Pub. L. 98-369, and the enactment of Pub. L. 99-121, such other Internal Revenue Code sections include sections 467, 483, 1274 and 7872. The order in which the different provisions shall be applied is as follows—

(i) First, the substance of the transaction shall be determined; for this purpose, all the relevant facts and circumstances shall be considered and any law or rule of law (assignment of income, step transaction, etc.) may apply. Only the rate of interest with respect to the stated principal amount of the bona fide indebtedness (within the meaning of paragraph (a)(1) of this section), if any, shall be subject to adjustment under section 482, paragraph (a) of this section, and any other Internal Revenue Code section.

(ii) Second, the other Internal Revenue Code section shall be applied to the loan or advance to determine whether any amount other than stated interest is to be treated as interest, and if so, to determine such amount according to the provisions of such other Internal Revenue Code section.

(iii) Third, whether or not the other Internal Revenue Code section applies to adjust the amounts treated as interest under such loan or advance, section 482 and paragraph (a) of this section may then be applied by the district director to determine whether the rate of interest charged on the loan or advance, as adjusted by any other Code section, is greater or less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

(iv) Fourth, section 482 and paragraphs (b) through (d) of this section and sections 1.482-3 through 1.482-7, if applicable, may be applied by the district director to make any appropriate allocations, other than an interest rate adjustment, to reflect an arm's length transaction based upon the principal amount of the loan or advance and the interest rate as adjusted under paragraph (a)(3)(i), (ii) or (iii) of this section. For example, assume that two commonly controlled taxpayers enter into a deferred payment sale of tangible property and no interest is provided, and assume also that section 483 is applied to treat a portion of the stated sales price as interest, thereby reducing the stated sales price. If after this recharacterization of a portion of the stated sales price as interest, the recomputed sales price does not reflect an arm's length sales price under the principles of section 1.482-3, the district director may make other appropriate allocations (other than an interest rate adjustment) to reflect an arm's length sales price.

(4) *Examples.* The principles of paragraph (a)(3) of this section may be illustrated by the following examples:

Example 1. An individual, A, transfers \$20,000 to a corporation controlled by A in exchange for the corporation's note which bears adequate stated interest. The district director recharacterizes the transaction as a contribution to the capital of the corporation in exchange for preferred stock. Under paragraph (a)(3)(i) of this section, section 1.482-2(a) does not apply to the transaction because there is no bona fide indebtedness.

Example 2. B, an individual, is an employee of Z corporation, and is also the controlling shareholder of Z. Z makes a term loan of \$15,000 to B at a rate of interest that is less than the applicable

Federal rate. In this instance the other operative Code section is section 7872. Under section 7872(b), the difference between the amount loaned and the present value of all payments due under the loan using a discount rate equal to 100 percent of the applicable Federal rate is treated as an amount of cash transferred from the corporation to B and the loan is treated as having original issue discount equal to such amount. Under paragraph (a)(3)(iii) of this section, section 482 and paragraph (a) of this section may also be applied by the district director to determine if the rate of interest charged on this \$15,000 loan (100 percent of the AFR, compounded semiannually, as adjusted by section 7872) is an arm's length rate of interest. Because the rate of interest on the loan, as adjusted by section 7872, is within the safe haven range of 100-130 percent of the AFR, compounded semiannually, no further interest rate adjustments under section 482 and paragraph (a) of this section will be made to this loan.

Example 3. The facts are the same as in Example 2 except that the amount lent by Z to B is \$9,000, and that amount is the aggregate outstanding amount of loans between Z and B. Under the \$10,000 de minimis exception of section 7872(c)(3), no adjustment for interest will be made to this \$9,000 loan under section 7872. Under paragraph (a)(3)(iii) of this section, the district director may apply section 482 and paragraph (a) of this section to this \$9,000 loan to determine whether the rate of interest charged is less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

Example 4. X and Y are commonly controlled taxpayers. At a time when the applicable Federal rate is 12 percent, compounded semiannually, X sells property to Y in exchange for a note with a stated rate of interest of 18 percent, compounded semiannually. Assume that the other applicable Code section to the transaction is section 483. Section 483 does not apply to this transaction because, under section 483(d), there is no total unstated interest under the contract using the test rate of interest equal to 100 percent of the applicable Federal rate. Under paragraph (a)(3)(iii) of this section, section 482 and paragraph (a) of this section may be applied by the district director to determine whether the rate of interest under the note is excessive, that is, to determine whether the 18 percent stated interest rate under the note exceeds an arm's length rate of interest.

Example 5. Assume that A and B are commonly controlled taxpayers and that the applicable Federal rate is 10 percent, compounded semiannually. On June 30, 1986, A sells property to B and receives in exchange B's purchase-money note in the amount of \$2,000,000. The stated interest rate on the note is 9%, compounded semiannually, and the stated redemption price at maturity on the note is \$2,000,000. Assume that the other applicable Code section to this transaction is section 1274. As provided in section 1274A(a) and (b), the discount rate for purposes of section 1274 will be nine percent, compounded semiannually, because the stated principal amount of B's note does not exceed \$2,800,000. Section 1274 does not apply to this transaction because there is adequate stated interest on the debt instrument using a discount rate equal to 9%, compounded semiannually, and the stated redemption price at maturity does not exceed the stated principal amount. Under paragraph (a)(3)(iii) of this section, the district director may apply section 482 and paragraph (a) of this section to this \$2,000,000 note to determine whether the 9% rate of interest charged is less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

(b) *Rendering of services.* For rules governing allocations under section 482 to reflect an arm's length charge for controlled transactions involving the rendering of services, see § 1.482-9.

(c) *Use of tangible property.*

(1) *General rule.* Where possession, use, or occupancy of tangible property owned or leased by one member of a group of controlled entities (referred to in this paragraph as the owner) is transferred by

lease or other arrangement to another member of such group (referred to in this paragraph as the user) without charge or at a charge which is not equal to an arm's length rental charge (as defined in paragraph (c)(2)(i) of this section) the district director may make appropriate allocations to properly reflect such arm's length charge. Where possession, use, or occupancy of only a portion of such property is transferred, the determination of the arm's length charge and the allocation shall be made with reference to the portion transferred.

(2) *Arm's length charge.*

(i) *In general.* For purposes of paragraph (c) of this section, an arm's length rental charge shall be the amount of rent which was charged, or would have been charged for the use of the same or similar property, during the time it was in use, in independent transactions with or between unrelated parties under similar circumstances considering the period and location of the use, the owner's investment in the property or rent paid for the property, expenses of maintaining the property, the type of property involved, its condition, and all other relevant facts.

(ii) *Safe haven rental charge.* See section 1.482-2(c)(2)(ii) (26 CFR Part 1 revised as of April 1, 1985), for the determination of safe haven rental charges in the case of certain leases entered into before May 9, 1986, and for leases entered into before August 7, 1986, pursuant to a binding written contract entered into before May 9, 1986.

(iii) *Subleases.*

(A) Except as provided in paragraph (c)(2)(iii)(B) of this section, where possession, use, or occupancy of tangible property, which is leased by the owner (lessee) from an unrelated party is transferred by sublease or other arrangement to the user, an arm's length rental charge shall be considered to be equal to all the deductions claimed by the owner (lessee) which are attributable to the property for the period such property is used by the user. Where only a portion of such property was transferred, any allocations shall be made with reference to the portion transferred. The deductions to be considered include the rent paid or accrued by the owner (lessee) during the period of use and all other deductions directly and indirectly connected with the property paid or accrued by the owner (lessee) during such period. Such deductions include deductions for maintenance and repair, utilities, management and other similar deductions.

(B) The provisions of paragraph (c)(2)(iii)(A) of this section shall not apply if either—

(1) The taxpayer establishes a more appropriate rental charge under the general rule set forth in paragraph (c)(2)(i) of this section; or

(2) During the taxable year, the owner (lessee) or the user was regularly engaged in the trade or business of renting property of the same general type as the property in question to unrelated persons.

(d) *Transfer of property.* For rules governing allocations under section 482 to reflect an arm's length consideration for controlled transactions involving the transfer of property, see sections 1.482-3 through 1.482-6.

(e) [Reserved]. For further guidance, see § 1.482-2T(e).

(f) *Effective/applicability date.*

(1) *In general.* The provision of paragraph (b) of this section is generally applicable for taxable years beginning after July 31, 2009.

(2) *Election to apply regulation to earlier taxable years.* A person may elect to apply the provisions of paragraph (b) of this section to earlier taxable years in accordance with the rules set forth in § 1.482-9(n)(2).

[T.D. 8552, 59 FR 34971-35030, July 8, 1994; corrected at 60 FR 16703, Mar. 31, 1995, and amended by T.D. 9278, 71 FR 44465-44519, Aug. 4, 2006; T.D. 9456, 74 FR 38829-38876, Aug. 4, 2009.]

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(a) through (d) [Reserved]. For further guidance, see § 1.482-2(a) through (d).

(e) *Cost sharing arrangement.* For rules governing allocations under section 482 to reflect an arm's length consideration for controlled transactions involving a cost sharing arrangement, see § 1.482-7T.

(f) *Effective/applicability date.*

(1) *In general.* The provision of paragraph (b) of this section is generally applicable for tax years beginning after December 31, 2006. The provision of paragraph (e) of this section is generally applicable on January 5, 2009.

(2) [Reserved]. For further guidance, see § 1.482-2(f)(2).

(3) *Ownership of intangible property.*

(i) *Identification of owner.*

(A) *In general.* The legal owner of intangible property pursuant to the intellectual property law of the relevant jurisdiction, or the holder of rights constituting an intangible property pursuant to contractual terms (such as the terms of a license) or other legal provision, will be considered the sole owner of the respective intangible property for purposes of this section unless such ownership is inconsistent with the economic substance of the underlying transactions. See § 1.482-1(d)(3)(ii)(B) (identifying contractual terms). If no owner of the respective intangible property is identified under the intellectual property law of the relevant jurisdiction, or pursuant to contractual terms (including terms imputed pursuant to § 1.482-1(d)(3)(ii)(B)) or other legal provision, then the controlled taxpayer who has control of the intangible property, based on all the facts and circumstances, will be considered the sole owner of the intangible property for purposes of this section.

(B) [Reserved]. For further guidance, see § 1.482-4T(f)(3)(i)(B).

(ii) *Examples.* The principles of this paragraph (f)(3) are illustrated by the following examples:

Example 1. FP, a foreign corporation, is the registered holder of the AA trademark in the United States. FP licenses to its U.S. subsidiary, USSub, the exclusive rights to manufacture and market products in the United States under the AA trademark. FP is the owner of the trademark pursuant to intellectual property law. USSub is the owner of the license pursuant to the terms of the license, but is not the owner of the trademark. See paragraphs (b)(3) and (4) of this section (defining an intangible as, among other things, a trademark or a license).

Example 2. The facts are the same as in Example 1. As a result of its sales and marketing activities, USSub develops a list of several hundred creditworthy customers that regularly purchase AA trademarked products. Neither the terms of the contract between FP and USSub nor the relevant intellectual property law specify which party owns the customer list. Because USSub has knowledge of the contents of the list, and has practical control over its use and dissemination, USSub is considered the sole owner of the customer list for purposes of this paragraph (f)(3).

(4) *Contribution to the value of intangible property owned by another.*

(i) *In general.* The arm's length consideration for a contribution by one controlled taxpayer that develops or enhances the value, or may be reasonably anticipated to develop or enhance the value, of intangible property owned by another controlled taxpayer will be determined in accordance with the applicable rules under section 482. If the consideration for such a contribution is embedded within the contractual terms for a controlled transaction that involves such intangible property, then ordinarily no separate allocation will be made with respect to such contribution. In such cases, pursuant to § 1.482-1(d)(3), the contribution must be accounted for in evaluating the comparability of the controlled transaction to uncontrolled comparables, and accordingly in determining the arm's length consideration in the controlled transaction.

(ii) *Examples.* The principles of this paragraph (f)(4) are illustrated by the following examples:

Example 1. A, a member of a controlled group, allows B, another member of the controlled group, to use tangible property, such as laboratory equipment, in connection with B's development of an intangible that B owns. By furnishing tangible property, A makes a contribution to the development of intangible property owned by another controlled taxpayer, B. Pursuant to paragraph (f)(4)(i) of this section, the arm's length charge for A's furnishing of tangible property will be determined under the rules for use of tangible property in § 1.482-2(c).

Example 2. (i) *Facts.* FP, a foreign producer of wristwatches, is the registered holder of the YY trademark in the United States and in other countries worldwide. FP enters into an exclusive, five-year, renewable agreement with its newly organized U.S. subsidiary, USSub. The contractual terms of the agreement grant USSub the exclusive right to re-sell YY trademark wristwatches in the United States, obligate USSub to pay a fixed price per wristwatch throughout the entire term of the contract, and obligate both FP and USSub to undertake without separate compensation specified types and levels of marketing activities.

(ii) The consideration for FP's and USSub's marketing activities, as well as the consideration for the exclusive right to re-sell YY trademarked merchandise in the United States, are embedded in the transfer price paid for the wristwatches. Accordingly, pursuant to paragraph (f)(4)(i) of this section, ordinarily no separate allocation would be appropriate with respect to these embedded contributions.

(iii) Whether an allocation is warranted with respect to the transfer price for the wristwatches is determined under §§ 1.482-1, 1.482-3, and this section through § 1.482-6. The comparability analysis would include consideration of all relevant factors, including the nature of the intangible property embedded in the wristwatches and the nature of the marketing activities required under the agreement. This analysis would also take into account that the compensation for the activities performed by USSub and FP, as well as the consideration for USSub's use of the YY trademark, is embedded in the transfer price for the wristwatches, rather than provided for in separate agreements. See §§ 1.482-3(f) and 1.482-9(m)(4).

Example 3. (i) *Facts.* FP, a foreign producer of athletic gear, is the registered holder of the AA trademark in the United States and in other countries. In year 1, FP licenses to a newly organized U.S. subsidiary, USSub, the exclusive rights to use certain manufacturing and marketing intangible property to manufacture and market athletic gear in the United States under the AA trademark. The license agreement obligates USSub to pay a royalty based on sales of trademarked merchandise. The license agreement also obligates FP and USSub to perform without separate compensation specified types and levels of marketing activities. In year 1, USSub manufactures and sells athletic gear under the AA trademark in the United States.

(ii) The consideration for FP's and USSub's respective marketing activities is embedded in the contractual terms of the license for the AA trademark. Accordingly, pursuant to paragraph (f)(4)(i)

of this section, ordinarily no separate allocation would be appropriate with respect to the embedded contributions in year 1. See § 1.482-9(m)(4).

(iii) Whether an allocation is warranted with respect to the royalty under the license agreement would be analyzed under § 1.482-1, and this section through § 1.482-6. The comparability analysis would include consideration of all relevant factors, such as the term and geographical exclusivity of the license, the nature of the intangible property subject to the license, and the nature of the marketing activities required to be undertaken pursuant to the license. Pursuant to paragraph (f)(4)(i) of this section, the analysis would also take into account the fact that the compensation for the marketing services is embedded in the royalty paid for use of the AA trademark, rather than provided for in a separate services agreement. For illustrations of application of the best method rule, see § 1.482-8 Examples 10, 11, and 12.

Example 4. (i) *Facts.* The year 1 facts are the same as in Example 3, with the following exceptions. In year 2, USSub undertakes certain incremental marketing activities in addition to those required by the contractual terms of the license for the AA trademark executed in year 1. The parties do not execute a separate agreement with respect to these incremental marketing activities performed by USSub. The license agreement executed in year 1 is of sufficient duration that it is reasonable to anticipate that USSub will obtain the benefit of its incremental activities, in the form of increased sales or revenues of trademarked products in the U.S. market.

(ii) To the extent that it was reasonable to anticipate that USSub's incremental marketing activities would increase the value only of USSub's intangible property (that is, USSub's license to use the AA trademark for a specified term), and not the value of the AA trademark owned by FP, USSub's incremental activities do not constitute a contribution for which an allocation is warranted under paragraph (f)(4)(i) of this section.

Example 5. (i) *Facts.* The year 1 facts are the same as in Example 3. In year 2, FP and USSub enter into a separate services agreement that obligates USSub to perform certain incremental marketing activities to promote AA trademark athletic gear in the United States, above and beyond the activities specified in the license agreement executed in year 1. In year 2, USSub begins to perform these incremental activities, pursuant to the separate services agreement with FP.

(ii) Whether an allocation is warranted with respect to USSub's incremental marketing activities covered by the separate services agreement would be evaluated under §§ 1.482-1 and 1.482-9, including a comparison of the compensation provided for the services with the results obtained under a method pursuant to § 1.482-9, selected and applied in accordance with the best method rule of § 1.482-1(c).

(iii) Whether an allocation is warranted with respect to the royalty under the license agreement is determined under § 1.482-1, and this section through § 1.482-6. The comparability analysis would include consideration of all relevant factors, such as the term and geographical exclusivity of the license, the nature of the intangible property subject to the license, and the nature of the marketing activities required to be undertaken pursuant to the license. The comparability analysis would take into account that the compensation for the incremental activities by USSub is provided for in the separate services agreement, rather than embedded in the royalty paid for use of the AA trademark. For illustrations of application of the best method rule, see § 1.482-8 Examples 10, 11, and 12.

Example 6. (i) *Facts.* The year 1 facts are the same as in Example 3. In year 2, FP and USSub enter into a separate services agreement that obligates FP to perform incremental marketing activities, not specified in the year 1 license, by advertising AA trademarked athletic gear in selected international sporting events, such as the Olympics and the soccer World Cup. FP's corporate advertising department develops and coordinates these special promotions. The separate services agreement obligates USSub to pay an amount to FP for the benefit to USSub that may reasonably be anticipated as the result of FP's incremental activities. The separate services agreement is not a qualified cost sharing arrangement

under § 1.482-7T. FP begins to perform the incremental activities in year 2 pursuant to the separate services agreement.

(ii) Whether an allocation is warranted with respect to the incremental marketing activities performed by FP under the separate services agreement would be evaluated under § 1.482-9. Under the circumstances, it is reasonable to anticipate that FP's activities would increase the value of USSub's license as well as the value of FP's trademark. Accordingly, the incremental activities by FP may constitute in part a controlled services transaction for which USSub must compensate FP. The analysis of whether an allocation is warranted would include a comparison of the compensation provided for the services with the results obtained under a method pursuant to § 1.482-9, selected and applied in accordance with the best method rule of § 1.482-1(c).

(iii) Whether an allocation is appropriate with respect to the royalty under the license agreement would be evaluated under §§ 1.482-1 through 1.482-3, this section, and §§ 1.482-5 and 1.482-6. The comparability analysis would include consideration of all relevant factors, such as the term and geographical exclusivity of USSub's license, the nature of the intangible property subject to the license, and the marketing activities required to be undertaken by both FP and USSub pursuant to the license. This comparability analysis would take into account that the compensation for the incremental activities performed by FP was provided for in the separate services agreement, rather than embedded in the royalty paid for use of the AA trademark. For illustrations of application of the best method rule, see § 1.482-8, Example 10, Example 11, and Example 12.

(g) [Reserved]. For further guidance, see § 1.482-4T(g).

(h) *Effective/applicability date.*

(1) *In general.* The provisions of paragraphs (f)(3)(i)(A), (f)(3)(ii), and (f)(4) of this section are generally applicable for taxable years beginning after July 31, 2009.

(2) *Election to apply regulation to earlier taxable years.* A person may elect to apply the provisions of paragraphs (f)(3)(i)(A), (f)(3)(ii), and (f)(4) of this section to earlier taxable years in accordance with the rules set forth in § 1.482-9(n)(2).

[Added by T.D. 9278, 71 FR 44465-44519, Aug. 4, 2006, as amended by T.D. 9441, 74 FR 340-391, Jan. 5, 2009; T.D. 9456, 74 FR 38829-38876, Aug. 4, 2009.]