

failure to provide information for purposes of paragraph (c)(4) of this section.

(3) *Information required*—(i) *Lessor*. The statement provided by the lessor must contain the lessor's name (and, in the case of a consolidated group, the parent's name), employer identification number, taxable year and the following information for each lease:

(A) The lessee's name (in the case of a consolidated group, the parent's name).

(B) The address of the lessee.

(C) The employer identification number of the lessee.

(D) The location of the retail space (including mall or strip center name, if applicable, and store name).

(E) The amount of the construction allowance.

(F) The amount of the construction allowance treated by the lessor as non-residential real property owned by the lessor.

(ii) *Lessee*. The statement provided by the lessee must contain the lessee's name (and, in the case of a consolidated group, the parent's name), employer identification number, taxable year and the following information for each lease:

(A) The lessor's name (in the case of a consolidated group, the parent's name).

(B) The address of the lessor.

(C) The employer identification number of the lessor.

(D) The location of the retail space (including mall or strip center name, if applicable, and store name).

(E) The amount of the construction allowance.

(F) The amount of the construction allowance that is a qualified lessee construction allowance under paragraph (b) of this section.

(4) *Failure to furnish information*. A lessor or a lessee that fails to furnish the information required in this paragraph (c) may be subject to a penalty under section 6721.

(d) *Effective date*. This section is applicable to leases entered into on or after October 5, 2000.

[T.D. 8901, 65 FR 53586, Sept. 5, 2000]

§ 1.111-1 Recovery of certain items previously deducted or credited.

(a) *General*. Section 111 provides that income attributable to the recovery during any taxable year of bad debts, prior taxes, and delinquency amounts shall be excluded from gross income to the extent of the "recovery exclusion" with respect to such items. The rule of exclusion so prescribed by statute applies equally with respect to all other losses, expenditures and accruals made the basis of deductions from gross income for prior taxable years, including war losses referred to in section 127 of the Internal Revenue Code of 1939, but not including deductions with respect to depreciation, depletion, amortization, or amortizable bond premiums. The term "recovery exclusion" as used in this section means an amount equal to the portion of the bad debts, prior taxes, and delinquency amounts (the items specifically referred to in section 111), and of all other items subject to the rule of exclusion which, when deducted or credited for a prior taxable year, did not result in a reduction of any tax of the taxpayer under subtitle A (other than the accumulated earnings tax imposed by section 531 or the personal holding company tax imposed by section 541) of the Internal Revenue Code of 1954 or corresponding provisions of prior income tax laws (other than the World War II excess profits tax imposed under subchapter E, chapter 2 of the Internal Revenue Code of 1939).

(1) *Section 111 items*. The term "section 111 items" as used in this section means bad debts, prior taxes, delinquency amounts, and all other items subject to the rule of exclusion, for which a deduction or credit was allowed for a prior taxable year. If a bad debt was previously charged against a reserve by a taxpayer on the reserve method of treating bad debts, it was not deducted, and it is therefore not considered a section 111 item. Bad debts, prior taxes, and delinquency amounts are defined in section 111(b) (1), (2), and (3), respectively. An example of a delinquency amount is interest on delinquent taxes. An example of the other items not expressly referred to in section 111 but nevertheless subject to the rule of exclusion is a loss sustained

upon the sale of stock and later recovered, in whole or in part, through an action against the party from whom such stock had been purchased.

(2) *Definition of "recovery"*. Recoveries result from the receipt of amounts in respect of the previously deducted or credited section 111 items, such as from the collection or sale of a bad debt, refund or credit of taxes paid, or cancellation of taxes accrued. Care should be taken in the case of bad debts which were treated as only partially worthless in prior years to distinguish between the item described in section 111, that is, the part of such debt which was deducted, and the part not previously deducted, which is not a section 111 item and is considered the first part collected. The collection of the part not deducted is not considered a "recovery". Furthermore, the term "recovery" does not include the gain resulting from the receipt of an amount on account of a section 111 item which, together with previous such receipts, exceeds the deduction or credit previously allowed for such item. For instance, a \$100 corporate bond purchased for \$40 and later deducted as worthless is subsequently collected to the extent of \$50. The \$10 gain (excess of \$50 collection over \$40 cost) is not a recovery of a section 111 item. Such gain is in no case excluded from gross income under section 111, regardless of whether the \$40 recovery is or is not excluded.

(3) *Treatment of debt deducted in more than one year by reason of partial worthlessness*. In the case of a bad debt deducted in part for two or more prior years, each such deduction of a part of the debt is considered a separate section 111 item. A recovery with respect to such debt is considered first a recovery of those items (or portions thereof), resulting from such debt, for which there are recovery exclusions. If there are recovery exclusions for two or more items resulting from the same bad debt, such items are considered recovered in the order of the taxable years for which they were deducted, beginning with the latest. The recovery exclusion for any such item is determined by considering the recovery exclusion with respect to the prior year for which such item was deducted as being first

used to offset all other applicable recoveries in the year in which the bad debt is recovered.

(4) *Special provisions as to worthless bonds, etc., which are treated as capital losses*. Certain bad debts arising from the worthlessness of securities and certain nonbusiness bad debts are treated as losses from the sale or exchange of capital assets. See sections 165(g) and 166(d). The amounts of the deductions allowed for any year under section 1211 on account of such losses for such year are considered to be section 111 items. Any part of such losses which, under section 1211, is a deduction for a subsequent year through the capital loss carryover (any later receipt of an amount with respect to such deducted loss is a recovery) is considered a section 111 item for the year in which such loss was sustained.

(b) *Computation of recovery exclusion—*
 (1) *Amount of recovery exclusion allowable for year of recovery*. For the year of any recovery, the section 111 items which were deducted or credited for one prior year are considered as a group and the recovery thereon is considered separately from recoveries of any items which were deducted or credited for other years. This recovery is excluded from gross income to the extent of the recovery exclusion with respect to this group of items as (i) determined for the original year for which such items were deducted or credited (see subparagraph (2) of this paragraph) and (ii) reduced by the excludable recoveries in intervening years on account of all section 111 items for such original year. A taxpayer claiming a recovery exclusion shall submit, at the time the exclusion is claimed, the computation of the recovery exclusion claimed for the original year for which the items were deducted or credited, and computations showing the amount recovered in intervening years on account of the section 111 items deducted or credited for the original year.

(2) *Determination of recovery exclusion for original year for which items were deducted or credited*. (i) The recovery exclusion for the taxable year for which section 111 items were deducted or credited (that is, the "original taxable year") is the portion of the aggregate amount of such deductions and credits

Internal Revenue Service, Treasury

§ 1.111-1

which could be disallowed without causing an increase in any tax of the taxpayer imposed under subtitle A (other than the accumulated earnings tax imposed by section 531 or the personal holding company tax imposed by section 541) of the Internal Revenue Code of 1954 or corresponding provisions of prior income tax laws (other than the World War II excess profits tax imposed under subchapter E, chapter 2 of the Internal Revenue Code of 1939). For the purpose of such recovery exclusion, consideration must be given to the effect of net operating loss carryovers and carrybacks or capital loss carryovers.

(ii) This rule shall be applied by determining the recovery exclusion as the aggregate amount of the section 111 items for the original year for which such items were deducted or credited reduced by whichever of the following amounts is the greater:

(a) The difference between (1) the taxable income for such original year and (2) the taxable income computed without regard to the section 111 items for such original year.

(b) In the case of a taxpayer subject to any income tax in lieu of normal tax or surtax or both (except the alternative tax on capital gains imposed by section 1201, which is disregarded), the difference between (1) the income subject to such tax for such original year and (2) the income subject to such tax computed without regard to the section 111 items for such original year.

(Neither the amount determined under (1) nor the amount under (2) of (a) or (b) of this subdivision shall in any case be considered less than zero.) For this determination of the recovery exclusion, the aggregate of the section 111 items must be further decreased by the portion thereof which caused a reduction in tax in preceding or succeeding taxable years through any net operating loss carryovers or carrybacks or capital loss carryovers affected by such items. This decrease is the aggregate of the largest amount determined for each of such preceding and succeeding years under (a) and (b) of this subdivision, the computation of each carryover or carryback to the preceding or succeeding year being made under (1) of (a) and (b) of this subdivision with

regard to the section 111 items for the original year and such computation being made under (2) of (a) and (b) of this subdivision without regard to such items. For the purpose of the preceding sentence, the computations under both (1) and (2) of (a) and (b) of this subdivision shall be made without regard to any section 111 items for such preceding or succeeding year and the carryovers and carrybacks to such year shall be determined without regard to any section 111 items for years subsequent to the original year.

(iii) The determination of the recovery exclusion for original taxable years subject to the provisions of the Internal Revenue Code of 1939 shall be made under 26 CFR (1939) 39.22(b)(12)-1(b)(2) (Regulations 118).

(3) *Example.* The provisions of this paragraph may be illustrated by the following example:

Example. A single individual with no dependents has for his 1954 taxable year the following income and deductions:

	With de- duction of section 111 items	Without deduc- tion of section 111 items
Gross income	\$25,000	\$25,000
Less deductions:		
Depreciation	20,000	20,000
Business bad debts and taxes	6,300
Personal exemption	600	600
	<hr/> 26,900	<hr/> 20,600
Taxable income or (loss)	(1,900)	4,400
Adjustment under section 172(d)(3)	600
	<hr/> (1,300)	<hr/>
Net operating loss	(1,300)

The full amount of the net operating loss of \$1,300 is carried back and allowed as a deduction for 1952. The aggregate of the section 111 items for 1954 is \$6,300 (bad debts and taxes). The recovery exclusion on account of section 111 items for 1954 is \$600, determined by reducing the \$6,300 aggregate of the section 111 items by \$5,700, i.e., the sum of (1) the difference between the amount of the taxable income for 1954 computed without regard to the section 111 items (\$4,400) and the amount of the taxable income for 1954 (not less than zero) computed by taking such items into account, and (2) the amount of the net operating loss (\$1,300) which caused the reduction in tax for 1952 by reason of the carryback provisions. If in 1956 the taxpayer recovers \$400 of the bad debts, all of the recovery is

§ 1.112-1

26 CFR Ch. I (4-1-04 Edition)

excluded from the income by reason of the recovery exclusion of \$600 determined for the original year 1954. If in 1957 the taxpayer recovers an additional \$300 of the bad debts, only \$200 is excluded from gross income. That is, the recovery exclusion of \$600 determined for the original year 1954 is reduced by the \$400 recovered in 1956, leaving a balance of \$200 which is used in 1957. The balance of the amount recovered in 1957, \$100 (\$300 less \$200), is included in gross income for 1957.

(c) *Provisions as to taxes imposed by section 531 (relating to the accumulated earnings tax) and section 541 (relating to the tax on personal holding companies).* A recovery exclusion allowed for purposes of subtitle A (other than section 531 or section 541) of the Internal Revenue Code of 1954 shall also be allowed for the purpose of determining the accumulated earnings tax under section 531 or the personal holding company tax under section 541 regardless of whether or not the section 111 items on which such recovery exclusion is based resulted in a reduction of the tax under section 531 or section 541 of the Internal Revenue Code of 1954 (or corresponding provisions of prior income tax laws) for the prior taxable year. Furthermore, if there is recovery of a section 111 item which was not allowable as a deduction or credit for the prior taxable year for purposes of Subtitle A (not including section 531 or section 541) or corresponding provisions of prior income tax laws (other than Subchapter E, Chapter 2 of the Internal Revenue Code of 1939, relating to World War II excess profits tax), but was allowable for such prior taxable year in determining the tax under section 531 or section 541 (or corresponding provisions of prior income tax laws) then for the purpose of determining the tax under section 531 or section 541 a recovery exclusion shall be allowable with respect to such recovery if the section 111 item did not result in a reduction of the tax under section 531 or section 541 (or corresponding provisions of prior income tax laws).

§ 1.112-1 Combat zone compensation of members of the Armed Forces.

(a) *Combat zone compensation exclusion—(1) Amount excluded.* In addition to the exemptions and credits otherwise applicable, section 112 excludes from gross income the following com-

ensation of members of the Armed Forces:

(i) *Enlisted personnel.* Compensation received for active service as a member below the grade of commissioned officer in the Armed Forces of the United States for any month during any part of which the member served in a combat zone or was hospitalized at any place as a result of wounds, disease, or injury incurred while serving in the combat zone.

(ii) *Commissioned officers.* Compensation not exceeding the monthly dollar limit received for active service as a commissioned officer in the Armed Forces of the United States for any month during any part of which the officer served in a combat zone or was hospitalized at any place as a result of wounds, disease, or injury incurred while serving in the combat zone. The monthly dollar limit is the monthly amount excludable from the officer's income under section 112(b) as amended. Beginning in 1966, the monthly dollar limit for periods of active service after 1965 became \$500. As of September 10, 1993, the monthly dollar limit continues to be \$500.

(2) *Time limits on exclusion during hospitalization.* Compensation received for service for any month of hospitalization that begins more than 2 years after the date specified by the President in an Executive Order as the date of the termination of combatant activities in the combat zone cannot be excluded under section 112. Furthermore, compensation received while hospitalized after January 1978 for wounds, disease, or injury incurred in the Vietnam combat zone designated by Executive Order 11216 cannot be excluded under section 112.

(3) *Special terms.* A commissioned warrant officer is not a *commissioned officer* under section 112(b) and is entitled to the exclusion allowed to enlisted personnel under section 112(a). *Compensation*, for the purpose of section 112, does not include pensions and retirement pay. *Armed Forces of the United States* is defined (and members of the Armed Forces are described) in section 7701(a)(15).

(4) *Military compensation only.* Only compensation paid by the Armed