

26 U.S. Code § 856 - Definition of real estate investment trust

Current through Pub. L. [114-38](#). (See [Public Laws for the current Congress](#).)

[US Code](#)[Notes](#)[IRS Rulings](#)[prev](#) | [next](#)

(a)IN GENERALFor purposes of this title, the term “real estate investment trust” means a corporation, trust, or association—

- (1)**which is managed by one or more trustees or directors;
- (2)**the beneficial ownership of which is evidenced by transferable shares, or by transferable certificates of beneficial interest;
- (3)**which (but for the provisions of this part) would be taxable as a domestic corporation;
- (4)**which is neither (A) a financial institution referred to in section 582(c)(2), nor (B) an insurance company to which subchapter L applies;
- (5)**the beneficial ownership of which is held by 100 or more persons;
- (6)**subject to the provisions of subsection (k), which is not closely held (as determined under subsection (h)); and
- (7)**which meets the requirements of subsection (c).

(b)DETERMINATION OF STATUS

The conditions described in paragraphs (1) to (4), inclusive, of subsection (a) must be met during the entire taxable year, and the condition described in paragraph (5) must exist during at least 335 days of a taxable year of 12 months, or during a proportionate part of a taxable year of less than 12 months.

(c)LIMITATIONSA corporation, trust, or association shall not be considered a real estate investment trust for any taxable year unless—

- (1)**it files with its return for the taxable year an election to be a real estate investment trust or has made such election for a previous taxable year, and such election has not been terminated or revoked under subsection (g);
- (2)**at least 95 percent (90 percent for taxable years beginning before January 1, 1980) of its gross income (excluding gross income from prohibited transactions) is derived from—
 - (A)**dividends;

(B)interest;

(C)rents from real property;

(D)gain from the sale or other disposition of stock, securities, and real property (including interests in real property and interests in mortgages on real property) which is not property described in section 1221(a)(1);

(E)abatements and refunds of taxes on real property;

(F)income and gain derived from foreclosure property (as defined in subsection (e));

(G)amounts (other than amounts the determination of which depends in whole or in part on the income or profits of any person) received or accrued as consideration for entering into agreements (i) to make loans secured by mortgages on real property or on interests in real property or (ii) to purchase or lease real property (including interests in real property and interests in mortgages on real property);

(H)gain from the sale or other disposition of a real estate asset which is not a prohibited transaction solely by reason of section 857(b)(6); and

(I)mineral royalty income earned in the first taxable year beginning after the date of the enactment of this subparagraph from real property owned by a timber real estate investment trust and held, or once held, in connection with the trade or business of producing timber by such real estate investment trust;

(3)at least 75 percent of its gross income (excluding gross income from prohibited transactions) is derived from—

(A)rents from real property;

(B)interest on obligations secured by mortgages on real property or on interests in real property;

(C)gain from the sale or other disposition of real property (including interests in real property and interests in mortgages on real property) which is not property described in section 1221(a)(1);

(D)dividends or other distributions on, and gain (other than gain from prohibited transactions) from the sale or other disposition of, transferable shares (or transferable certificates of beneficial interest) in other real estate investment trusts which meet the requirements of this part;

(E)abatements and refunds of taxes on real property;

(F)income and gain derived from foreclosure property (as defined in

subsection (e));

(G) amounts (other than amounts the determination of which depends in whole or in part on the income or profits of any person) received or accrued as consideration for entering into agreements (i) to make loans secured by mortgages on real property or on interests in real property or (ii) to purchase or lease real property (including interests in real property and interests in mortgages on real property);

(H) gain from the sale or other disposition of a real estate asset which is not a prohibited transaction solely by reason of section 857(b)(6); and

(I) qualified temporary investment income; and

(4) at the close of each quarter of the taxable year—

(A) at least 75 percent of the value of its total assets is represented by real estate assets, cash and cash items (including receivables), and Government securities; and

(B)

(i) not more than 25 percent of the value of its total assets is represented by securities (other than those includible under subparagraph (A)),

(ii) not more than 25 percent of the value of its total assets is represented by securities of one or more taxable REIT subsidiaries,^{[11](#)}

(iii) except with respect to a taxable REIT subsidiary and securities includible under subparagraph (A)—

(I) not more than 5 percent of the value of its total assets is represented by securities of any one issuer,

(II) the trust does not hold securities possessing more than 10 percent of the total voting power of the outstanding securities of any one issuer, and

(III) the trust does not hold securities having a value of more than 10 percent of the total value of the outstanding securities of any one issuer.

A real estate investment trust which meets the requirements of this paragraph at the close of any quarter shall not lose its status as a real estate investment trust because of a discrepancy during a subsequent quarter between the value of its various investments and such requirements (including a discrepancy caused solely by the change in the foreign currency exchange rate used to value a foreign asset) unless such discrepancy exists immediately after the

acquisition of any security or other property and is wholly or partly the result of such acquisition. A real estate investment trust which does not meet such requirements at the close of any quarter by reason of a discrepancy existing immediately after the acquisition of any security or other property which is wholly or partly the result of such acquisition during such quarter shall not lose its status for such quarter as a real estate investment trust if such discrepancy is eliminated within 30 days after the close of such quarter and in such cases it shall be considered to have met such requirements at the close of such quarter for purposes of applying the preceding sentence.

(5)For purposes of this part—

(A)The term “value” means, with respect to securities for which market quotations are readily available, the market value of such securities; and with respect to other securities and assets, fair value as determined in good faith by the trustees, except that in the case of securities of real estate investment trusts such fair value shall not exceed market value or asset value, whichever is higher.

(B)The term “real estate assets” means real property (including interests in real property and interests in mortgages on real property) and shares (or transferable certificates of beneficial interest) in other real estate investment trusts which meet the requirements of this part. Such term also includes any property (not otherwise a real estate asset) attributable to the temporary investment of new capital, but only if such property is stock or a debt instrument, and only for the 1-year period beginning on the date the real estate trust receives such capital.

(C)The term “interests in real property” includes fee ownership and co-ownership of land or improvements thereon, leaseholds of land or improvements thereon, options to acquire land or improvements thereon, and options to acquire leaseholds of land or improvements thereon, but does not include mineral, oil, or gas royalty interests.

(D)Qualified temporary investment income.—

(i)In general.—The term “qualified temporary investment income” means any income which—

(I)is attributable to stock or a debt instrument (within the meaning of section 1275(a)(1)),

(II)is attributable to the temporary investment of new capital, and

(III)is received or accrued during the 1-year period beginning on the date on which the real estate investment trust receives such capital.

(ii)New capital.—The term “new capital” means any amount received by

the real estate investment trust—

(I)in exchange for stock (or certificates of beneficial interests) in such trust (other than amounts received pursuant to a dividend reinvestment plan), or

(II)in a public offering of debt obligations of such trust which have maturities of at least 5 years.

(E)A regular or residual interest in a REMIC shall be treated as a real estate asset, and any amount includible in gross income with respect to such an interest shall be treated as interest on an obligation secured by a mortgage on real property; except that, if less than 95 percent of the assets of such REMIC are real estate assets (determined as if the real estate investment trust held such assets), such real estate investment trust shall be treated as holding directly (and as receiving directly) its proportionate share of the assets and income of the REMIC. For purposes of determining whether any interest in a REMIC qualifies under the preceding sentence, any interest held by such REMIC in another REMIC shall be treated as a real estate asset under principles similar to the principles of the preceding sentence, except that, if such REMIC's are part of a tiered structure, they shall be treated as one REMIC for purposes of this subparagraph.

(F)All other terms shall have the same meaning as when used in the Investment Company Act of 1940, as amended ([15 U.S.C. 80a-1](#) and following).

(G)Treatment of certain hedging instruments.—Except to the extent as determined by the Secretary—

(i)any income of a real estate investment trust from a hedging transaction (as defined in clause (ii) or (iii) of section 1221(b)(2)(A)) which is clearly identified pursuant to section 1221(a)(7), including gain from the sale or disposition of such a transaction, shall not constitute gross income under paragraphs (2) and (3) to the extent that the transaction hedges any indebtedness incurred or to be incurred by the trust to acquire or carry real estate assets, and

(ii)any income of a real estate investment trust from a transaction entered into by the trust primarily to manage risk of currency fluctuations with respect to any item of income or gain described in paragraph (2) or (3) (or any property which generates such income or gain), including gain from the termination of such a transaction, shall not constitute gross income under paragraphs (2) and (3), but only if such transaction is clearly identified as such before the close of the day on which it was acquired, originated, or entered into (or such other time as the Secretary may prescribe).

(H) Treatment of timber gains.—

(i) In general.—Gain from the sale of real property described in paragraph (2)(D) and (3)(C) shall include gain which is—

(I) recognized by an election under section 631(a) from timber owned by the real estate investment trust, the cutting of which is provided by a taxable REIT subsidiary of the real estate investment trust;

(II) recognized under section 631(b); or

(III) income which would constitute gain under subclause (I) or (II) but for the failure to meet the 1-year holding period requirement.

(ii) Special rules.—

(I) For purposes of this subtitle, cut timber, the gain from which is recognized by a real estate investment trust pursuant to an election under section 631(a) described in clause (i)(I) or so much of clause (i)(III) as relates to clause (i)(I), shall be deemed to be sold to the taxable REIT subsidiary of the real estate investment trust on the first day of the taxable year.

(II) For purposes of this subtitle, income described in this subparagraph shall not be treated as gain from the sale of property described in section 1221(a)(1).

(iii) Termination.—

This subparagraph shall not apply to dispositions after the termination date.

(I) Timber real estate investment trust.—

The term “timber real estate investment trust” means a real estate investment trust in which more than 50 percent in value of its total assets consists of real property held in connection with the trade or business of producing timber.

(J) Secretarial authority to exclude other items of income.—To the extent necessary to carry out the purposes of this part, the Secretary is authorized to determine, solely for purposes of this part, whether any item of income or gain which—

(i) does not otherwise qualify under paragraph (2) or (3) may be considered as not constituting gross income for purposes of paragraphs (2) or (3), or

(ii) otherwise constitutes gross income not qualifying under paragraph (2) or (3) may be considered as gross income which qualifies under

paragraph (2) or (3).

(K)Cash.—If the real estate investment trust or its qualified business unit (as defined in section 989) uses any foreign currency as its functional currency (as defined in section 985(b)), the term “cash” includes such foreign currency but only to the extent such foreign currency—

(i) is held for use in the normal course of the activities of the trust or qualified business unit which give rise to items of income or gain described in paragraph (2) or (3) of subsection (c) or are directly related to acquiring or holding assets described in subsection (c)(4), and

(ii) is not held in connection with an activity described in subsection (n) (4).

(6)A corporation, trust, or association which fails to meet the requirements of paragraph (2) or (3), or of both such paragraphs, for any taxable year shall nevertheless be considered to have satisfied the requirements of such paragraphs for such taxable year if—

(A) following the corporation, trust, or association’s identification of the failure to meet the requirements of paragraph (2) or (3), or of both such paragraphs, for any taxable year, a description of each item of its gross income described in such paragraphs is set forth in a schedule for such taxable year filed in accordance with regulations prescribed by the Secretary, and

(B) the failure to meet the requirements of paragraph (2) or (3), or of both such paragraphs, is due to reasonable cause and not due to willful neglect.

(7)RULES OF APPLICATION FOR FAILURE TO SATISFY PARAGRAPH (4).—

(A)In general.—A corporation, trust, or association that fails to meet the requirements of paragraph (4) (other than a failure to meet the requirements of paragraph (4)(B)(iii) which is described in subparagraph (B)(i) of this paragraph) for a particular quarter shall nevertheless be considered to have satisfied the requirements of such paragraph for such quarter if—

(i) following the corporation, trust, or association’s identification of the failure to satisfy the requirements of such paragraph for a particular quarter, a description of each asset that causes the corporation, trust, or association to fail to satisfy the requirements of such paragraph at the close of such quarter of any taxable year is set forth in a schedule for such quarter filed in accordance with regulations prescribed by the Secretary,

(ii) the failure to meet the requirements of such paragraph for a particular quarter is due to reasonable cause and not due to willful neglect, and

(iii)

(I)the corporation, trust, or association disposes of the assets set forth on the schedule specified in clause (i) within 6 months after the last day of the quarter in which the corporation, trust or association's identification of the failure to satisfy the requirements of such paragraph occurred or such other time period prescribed by the Secretary and in the manner prescribed by the Secretary, or

(II)the requirements of such paragraph are otherwise met within the time period specified in subclause (I).

(B)Rule for certain de minimis failures.—A corporation, trust, or association that fails to meet the requirements of paragraph (4)(B)(iii) for a particular quarter shall nevertheless be considered to have satisfied the requirements of such paragraph for such quarter if—

(i)such failure is due to the ownership of assets the total value of which does not exceed the lesser of—

(I)1 percent of the total value of the trust's assets at the end of the quarter for which such measurement is done, and

(II)\$10,000,000, and

(ii)

(I)the corporation, trust, or association, following the identification of such failure, disposes of assets in order to meet the requirements of such paragraph within 6 months after the last day of the quarter in which the corporation, trust or association's identification of the failure to satisfy the requirements of such paragraph occurred or such other time period prescribed by the Secretary and in the manner prescribed by the Secretary, or

(II)the requirements of such paragraph are otherwise met within the time period specified in subclause (I).

(C)Tax.—

(i)Tax imposed.—If subparagraph (A) applies to a corporation, trust, or association for any taxable year, there is hereby imposed on such corporation, trust, or association a tax in an amount equal to the greater of—

(I)\$50,000, or

(II)the amount determined (pursuant to regulations promulgated by the Secretary) by multiplying the net income generated by the assets

described in the schedule specified in subparagraph (A)(i) for the period specified in clause (ii) by the highest rate of tax specified in section 11.

(ii)Period.—

For purposes of clause (i)(II), the period described in this clause is the period beginning on the first date that the failure to satisfy the requirements of such paragraph (4) occurs as a result of the ownership of such assets and ending on the earlier of the date on which the trust disposes of such assets or the end of the first quarter when there is no longer a failure to satisfy such paragraph (4).

(iii)Administrative provisions.—

For purposes of subtitle F, the taxes imposed by this subparagraph shall be treated as excise taxes with respect to which the deficiency procedures of such subtitle apply.

(8)TERMINATION DATE.—

For purposes of this subsection, the term “termination date” means, with respect to any taxpayer, the last day of the taxpayer’s first taxable year beginning after the date of the enactment of this paragraph and before the date that is 1 year after such date of enactment.

(d)RENTS FROM REAL PROPERTY DEFINED

(1)AMOUNTS INCLUDEDFor purposes of paragraphs (2) and (3) of subsection (c), the term “rents from real property” includes (subject to paragraph (2))—

(A)rents from interests in real property,

(B)charges for services customarily furnished or rendered in connection with the rental of real property, whether or not such charges are separately stated, and

(C)rent attributable to personal property which is leased under, or in connection with, a lease of real property, but only if the rent attributable to such personal property for the taxable year does not exceed 15 percent of the total rent for the taxable year attributable to both the real and personal property leased under, or in connection with, such lease.

For purposes of subparagraph (C), with respect to each lease of real property, rent attributable to personal property for the taxable year is that amount which bears the same ratio to total rent for the taxable year as the average of the fair market values of the personal property at the beginning and at the end of the taxable year bears to the average of the aggregate fair market values of both the real property and the personal property at the beginning and at the end of such taxable year.

(2) AMOUNTS EXCLUDED For purposes of paragraphs (2) and (3) of subsection (c), the term “rents from real property” does not include—

(A) except as provided in paragraphs (4) and (6), any amount received or accrued, directly or indirectly, with respect to any real or personal property, if the determination of such amount depends in whole or in part on the income or profits derived by any person from such property (except that any amount so received or accrued shall not be excluded from the term “rents from real property” solely by reason of being based on a fixed percentage or percentages of receipts or sales);

(B) except as provided in paragraph (8), any amount received or accrued directly or indirectly from any person if the real estate investment trust owns, directly or indirectly—

(i) in the case of any person which is a corporation, stock of such person possessing 10 percent or more of the total combined voting power of all classes of stock entitled to vote, or 10 percent or more of the total value of shares of all classes of stock of such person; or

(ii) in the case of any person which is not a corporation, an interest of 10 percent or more in the assets or net profits of such person; and

(C) any impermissible tenant service income (as defined in paragraph (7)).

(3) INDEPENDENT CONTRACTOR DEFINED For purposes of this subsection and subsection (e), the term “independent contractor” means any person—

(A) who does not own, directly or indirectly, more than 35 percent of the shares, or certificates of beneficial interest, in the real estate investment trust; and

(B) if such person is a corporation, not more than 35 percent of the total combined voting power of whose stock (or 35 percent of the total shares of all classes of whose stock), or, if such person is not a corporation, not more than 35 percent of the interest in whose assets or net profits is owned, directly or indirectly, by one or more persons owning 35 percent or more of the shares or certificates of beneficial interest in the trust.

In the event that any class of stock of either the real estate investment trust or such person is regularly traded on an established securities market, only persons who own, directly or indirectly, more than 5 percent of such class of stock shall be taken into account as owning any of the stock of such class for purposes of applying the 35 percent limitation set forth in subparagraph (B) (but all of the outstanding stock of such class shall be considered outstanding in order to compute the denominator for purpose of determining the applicable percentage of ownership).

(4) SPECIAL RULE FOR CERTAIN CONTINGENT RENTS

Where a real estate investment trust receives or accrues, with respect to real or personal property, any amount which would be excluded from the term "rents from real property" solely because the tenant of the real estate investment trust receives or accrues, directly or indirectly, from subtenants any amount the determination of which depends in whole or in part on the income or profits derived by any person from such property, only a proportionate part (determined pursuant to regulations prescribed by the Secretary) of the amount received or accrued by the real estate investment trust from that tenant will be excluded from the term "rents from real property".

(5) CONSTRUCTIVE OWNERSHIP OF STOCK For purposes of this subsection, the rules prescribed by section 318(a) for determining the ownership of stock shall apply in determining the ownership of stock, assets, or net profits of any person; except that—

(A) "10 percent" shall be substituted for "50 percent" in subparagraph (C) of paragraphs (2) and (3) of section 318(a), and

(B) section 318(a)(3)(A) shall be applied in the case of a partnership by taking into account only partners who own (directly or indirectly) 25 percent or more of the capital interest, or the profits interest, in the partnership.

(6) SPECIAL RULE FOR CERTAIN PROPERTY SUBLEASED BY TENANT OF REAL ESTATE INVESTMENT TRUSTS**(A) In general** If—

(i) a real estate investment trust receives or accrues, with respect to real or personal property, amounts from a tenant which derives substantially all of its income with respect to such property from the subleasing of substantially all of such property, and

(ii) a portion of the amount such tenant receives or accrues, directly or indirectly, from subtenants consists of qualified rents,

then the amounts which the trust receives or accrues from the tenant shall not be excluded from the term "rents from real property" by reason of being based on the income or profits of such tenant to the extent the amounts so received or accrued are attributable to qualified rents received or accrued by such tenant.

(B) Qualified rents

For purposes of subparagraph (A), the term "qualified rents" means any amount which would be treated as rents from real property if received by the real estate investment trust.

(7) IMPERMISSIBLE TENANT SERVICE INCOME For purposes of paragraph (2)(C)—

(A) In general The term “impermissible tenant service income” means, with respect to any real or personal property, any amount received or accrued directly or indirectly by the real estate investment trust for—

- (i)** services furnished or rendered by the trust to the tenants of such property, or
- (ii)** managing or operating such property.

(B) Disqualification of all amounts where more than de minimis amount

If the amount described in subparagraph (A) with respect to a property for any taxable year exceeds 1 percent of all amounts received or accrued during such taxable year directly or indirectly by the real estate investment trust with respect to such property, the impermissible tenant service income of the trust with respect to the property shall include all such amounts.

(C) Exceptions For purposes of subparagraph (A)—

- (i)** services furnished or rendered, or management or operation provided, through an independent contractor from whom the trust itself does not derive or receive any income or through a taxable REIT subsidiary of such trust shall not be treated as furnished, rendered, or provided by the trust, and
- (ii)** there shall not be taken into account any amount which would be excluded from unrelated business taxable income under section 512(b)(3) if received by an organization described in section 511(a)(2).

(D) Amount attributable to impermissible services

For purposes of subparagraph (A), the amount treated as received for any service (or management or operation) shall not be less than 150 percent of the direct cost of the trust in furnishing or rendering the service (or providing the management or operation).

(E) Coordination with limitations

For purposes of paragraphs (2) and (3) of subsection (c), amounts described in subparagraph (A) shall be included in the gross income of the corporation, trust, or association.

(8) SPECIAL RULE FOR TAXABLE REIT SUBSIDIARIES For purposes of this subsection, amounts paid to a real estate investment trust by a taxable REIT subsidiary of such trust shall not be excluded from rents from real property by reason of paragraph (2)(B) if the requirements of either of the following subparagraphs are

met:

(A)Limited rental exception

(i)In general

The requirements of this subparagraph are met with respect to any property if at least 90 percent of the leased space of the property is rented to persons other than taxable REIT subsidiaries of such trust and other than persons described in paragraph (2)(B).

(ii)Rents must be substantially comparable

Clause (i) shall apply only to the extent that the amounts paid to the trust as rents from real property (as defined in paragraph (1) without regard to paragraph (2)(B)) from such property are substantially comparable to such rents paid by the other tenants of the trust's property for comparable space.

(iii)Times for testing rent comparabilityThe substantial comparability requirement of clause (ii) shall be treated as met with respect to a lease to a taxable REIT subsidiary of the trust if such requirement is met under the terms of the lease—

(I)at the time such lease is entered into,

(II)at the time of each extension of the lease, including a failure to exercise a right to terminate, and

(III)at the time of any modification of the lease between the trust and the taxable REIT subsidiary if the rent under such lease is effectively increased pursuant to such modification.

With respect to subclause (III), if the taxable REIT subsidiary of the trust is a controlled taxable REIT subsidiary of the trust, the term "rents from real property" shall not in any event include rent under such lease to the extent of the increase in such rent on account of such modification.

(iv)Controlled taxable REIT subsidiaryFor purposes of clause (iii), the term "controlled taxable REIT subsidiary" means, with respect to any real estate investment trust, any taxable REIT subsidiary of such trust if such trust owns directly or indirectly—

(I)stock possessing more than 50 percent of the total voting power of the outstanding stock of such subsidiary, or

(II)stock having a value of more than 50 percent of the total value of the outstanding stock of such subsidiary.

(v)Continuing qualification based on third party actions

If the requirements of clause (i) are met at a time referred to in clause (iii), such requirements shall continue to be treated as met so long as there is no increase in the space leased to any taxable REIT subsidiary of such trust or to any person described in paragraph (2)(B).

(vi) Correction period

If there is an increase referred to in clause (v) during any calendar quarter with respect to any property, the requirements of clause (iii) shall be treated as met during the quarter and the succeeding quarter if such requirements are met at the close of such succeeding quarter.

(B) Exception for certain lodging facilities and health care property The requirements of this subparagraph are met with respect to an interest in real property which is a qualified lodging facility (as defined in paragraph (9)(D)) or a qualified health care property (as defined in subsection (e)(6)(D)(i)) leased by the trust to a taxable REIT subsidiary of the trust if the property is operated on behalf of such subsidiary by a person who is an eligible independent contractor. For purposes of this section, a taxable REIT subsidiary is not considered to be operating or managing a qualified health care property or qualified lodging facility solely because it—

(i) directly or indirectly possesses a license, permit, or similar instrument enabling it to do so, or

(ii) employs individuals working at such facility or property located outside the United States, but only if an eligible independent contractor is responsible for the daily supervision and direction of such individuals on behalf of the taxable REIT subsidiary pursuant to a management agreement or similar service contract.

(9) ELIGIBLE INDEPENDENT CONTRACTOR For purposes of paragraph (8)(B)—

(A) In general

The term “eligible independent contractor” means, with respect to any qualified lodging facility or qualified health care property (as defined in subsection (e)(6)(D)(i)), any independent contractor if, at the time such contractor enters into a management agreement or other similar service contract with the taxable REIT subsidiary to operate such qualified lodging facility or qualified health care property, such contractor (or any related person) is actively engaged in the trade or business of operating qualified lodging facilities or qualified health care properties, respectively, for any person who is not a related person with respect to the real estate investment trust or the taxable REIT subsidiary.

(B) Special rules Solely for purposes of this paragraph and paragraph (8)(B),

a person shall not fail to be treated as an independent contractor with respect to any qualified lodging facility or qualified health care property (as so defined) by reason of the following:

(i)The taxable REIT subsidiary bears the expenses for the operation of such qualified lodging facility or qualified health care property pursuant to the management agreement or other similar service contract.

(ii)The taxable REIT subsidiary receives the revenues from the operation of such qualified lodging facility or qualified health care property, net of expenses for such operation and fees payable to the operator pursuant to such agreement or contract.

(iii)The real estate investment trust receives income from such person with respect to another property that is attributable to a lease of such other property to such person that was in effect as of the later of—

(I)January 1, 1999, or

(II)the earliest date that any taxable REIT subsidiary of such trust entered into a management agreement or other similar service contract with such person with respect to such qualified lodging facility or qualified health care property.

(C)Renewals, etc., of existing leasesFor purposes of subparagraph (B)(iii)

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(i)a lease shall be treated as in effect on January 1, 1999, without regard to its renewal after such date, so long as such renewal is pursuant to the terms of such lease as in effect on whichever of the dates under subparagraph (B)(iii) is the latest, and

(ii)a lease of a property entered into after whichever of the dates under subparagraph (B)(iii) is the latest shall be treated as in effect on such date if—

(I)on such date, a lease of such property from the trust was in effect, and

(II)under the terms of the new lease, such trust receives a substantially similar or lesser benefit in comparison to the lease referred to in subclause (I).

(D)Qualified lodging facilityFor purposes of this paragraph—

(i)In general

The term “qualified lodging facility” means any lodging facility unless wagering activities are conducted at or in connection with such facility by

any person who is engaged in the business of accepting wagers and who is legally authorized to engage in such business at or in connection with such facility.

(ii)Lodging facilityThe term “lodging facility” means a—

(I)hotel,

(II)motel, or

(III)other establishment more than one-half of the dwelling units in which are used on a transient basis.

(iii)Customary amenities and facilities

The term “lodging facility” includes customary amenities and facilities operated as part of, or associated with, the lodging facility so long as such amenities and facilities are customary for other properties of a comparable size and class owned by other owners unrelated to such real estate investment trust.

(E)Operate includes manage

References in this paragraph to operating a property shall be treated as including a reference to managing the property.

(F)Related person

Persons shall be treated as related to each other if such persons are treated as a single employer under subsection (a) or (b) of section 52.

(e)SPECIAL RULES FOR FORECLOSURE PROPERTY

(1)FORECLOSURE PROPERTY DEFINED

For purposes of this part, the term “foreclosure property” means any real property (including interests in real property), and any personal property incident to such real property, acquired by the real estate investment trust as the result of such trust having bid in such property at foreclosure, or having otherwise reduced such property to ownership or possession by agreement or process of law, after there was default (or default was imminent) on a lease of such property or on an indebtedness which such property secured. Such term does not include property acquired by the real estate investment trust as a result of indebtedness arising from the sale or other disposition of property of the trust described in section 1221(a)(1) which was not originally acquired as foreclosure property.

(2)GRACE PERIOD

Except as provided in paragraph (3), property shall cease to be foreclosure

property with respect to the real estate investment trust as of the close of the 3d taxable year following the taxable year in which the trust acquired such property.

(3) EXTENSIONS

If the real estate investment trust establishes to the satisfaction of the Secretary that an extension of the grace period is necessary for the orderly liquidation of the trust's interests in such property, the Secretary may grant one extension of the grace period for such property. Any such extension shall not extend the grace period beyond the close of the 3d taxable year following the last taxable year in the period under paragraph (2).

(4) TERMINATION OF GRACE PERIOD IN CERTAIN CASES Any foreclosure property shall cease to be such on the first day (occurring on or after the day on which the real estate investment trust acquired the property) on which—

(A) a lease is entered into with respect to such property which, by its terms, will give rise to income which is not described in subsection (c)(3) (other than subparagraph (F) of such subsection), or any amount is received or accrued, directly or indirectly, pursuant to a lease entered into on or after such day which is not described in such subsection,

(B) any construction takes place on such property (other than completion of a building, or completion of any other improvement, where more than 10 percent of the construction of such building or other improvement was completed before default became imminent), or

(C) if such day is more than 90 days after the day on which such property was acquired by the real estate investment trust and the property is used in a trade or business which is conducted by the trust (other than through an independent contractor (within the meaning of section (d)(3)) from whom the trust itself does not derive or receive any income).

For purposes of subparagraph (C), property shall not be treated as used in a trade or business by reason of any activities of the real estate investment trust with respect to such property to the extent that such activities would not result in amounts received or accrued, directly or indirectly, with respect to such property being treated as other than rents from real property.

(5) TAXPAYER MUST MAKE ELECTION

Property shall be treated as foreclosure property for purposes of this part only if the real estate investment trust so elects (in the manner provided in regulations prescribed by the Secretary) on or before the due date (including any extensions of time) for filing its return of tax under this chapter for the taxable year in which such trust acquires such property. A real estate investment trust may revoke any such election for a taxable year by filing the revocation (in the manner provided by the Secretary) on or before the due date (including any extension of time) for

filing its return of tax under this chapter for the taxable year. If a trust revokes an election for any property, no election may be made by the trust under this paragraph with respect to the property for any subsequent taxable year.

(6) SPECIAL RULE FOR QUALIFIED HEALTH CARE PROPERTIES For purposes of this subsection—

(A) Acquisition at expiration of lease

The term “foreclosure property” shall include any qualified health care property acquired by a real estate investment trust as the result of the termination of a lease of such property (other than a termination by reason of a default, or the imminence of a default, on the lease).

(B) Grace period In the case of a qualified health care property which is foreclosure property solely by reason of subparagraph (A), in lieu of applying paragraphs (2) and (3)—

(i) the qualified health care property shall cease to be foreclosure property as of the close of the second taxable year after the taxable year in which such trust acquired such property, and

(ii) if the real estate investment trust establishes to the satisfaction of the Secretary that an extension of the grace period in clause (i) is necessary to the orderly leasing or liquidation of the trust’s interest in such qualified health care property, the Secretary may grant one or more extensions of the grace period for such qualified health care property.

Any such extension shall not extend the grace period beyond the close of the 6th year after the taxable year in which such trust acquired such qualified health care property.

(C) Income from independent contractors For purposes of applying paragraph (4)(C) with respect to qualified health care property which is foreclosure property by reason of subparagraph (A) or paragraph (1), income derived or received by the trust from an independent contractor shall be disregarded to the extent such income is attributable to—

(i) any lease of property in effect on the date the real estate investment trust acquired the qualified health care property (without regard to its renewal after such date so long as such renewal is pursuant to the terms of such lease as in effect on such date), or

(ii) any lease of property entered into after such date if—

(I) on such date, a lease of such property from the trust was in effect, and

(II) under the terms of the new lease, such trust receives a substantially similar or lesser benefit in comparison to the lease

referred to in subclause (I).

(D) Qualified health care property

(i) In general The term “qualified health care property” means any real property (including interests therein), and any personal property incident to such real property, which—

(I) is a health care facility, or

(II) is necessary or incidental to the use of a health care facility.

(ii) Health care facility

For purposes of clause (i), the term “health care facility” means a hospital, nursing facility, assisted living facility, congregate care facility, qualified continuing care facility (as defined in section 7872(g)(4)), or other licensed facility which extends medical or nursing or ancillary services to patients and which, immediately before the termination, expiration, default, or breach of the lease of or mortgage secured by such facility, was operated by a provider of such services which was eligible for participation in the medicare program under title XVIII of the Social Security Act with respect to such facility.

(f) INTEREST

(1) IN GENERAL For purposes of paragraphs (2)(B) and (3)(B) of subsection (c), the term “interest” does not include any amount received or accrued, directly or indirectly, if the determination of such amount depends in whole or in part on the income or profits of any person except that—

(A) any amount so received or accrued shall not be excluded from the term “interest” solely by reason of being based on a fixed percentage or percentages of receipts or sales, and

(B) where a real estate investment trust receives any amount which would be excluded from the term “interest” solely because the debtor of the real estate investment trust receives or accrues any amount the determination of which depends in whole or in part on the income or profits of any person, only a proportionate part (determined pursuant to regulations prescribed by the Secretary) of the amount received or accrued by the real estate investment trust from the debtor will be excluded from the term “interest”.

(2) SPECIAL RULE If—

(A) a real estate investment trust receives or accrues with respect to an obligation secured by a mortgage on real property or an interest in real

property amounts from a debtor which derives substantially all of its gross income with respect to such property (not taking into account any gain on any disposition) from the leasing of substantially all of its interests in such property to tenants, and

(B)a portion of the amount which such debtor receives or accrues, directly or indirectly, from tenants consists of qualified rents (as defined in subsection (d)(6)(B)),

then the amounts which the trust receives or accrues from such debtor shall not be excluded from the term "interest" by reason of being based on the income or profits of such debtor to the extent the amounts so received are attributable to qualified rents received or accrued by such debtor.

(g)TERMINATION OF ELECTION

(1)FAILURE TO QUALIFY

An election under subsection (c)(1) made by a corporation, trust, or association shall terminate if the corporation, trust, or association is not a real estate investment trust to which the provisions of this part apply for the taxable year with respect to which the election is made, or for any succeeding taxable year unless paragraph (5) applies. Such termination shall be effective for the taxable year for which the corporation, trust, or association is not a real estate investment trust to which the provisions of this part apply, and for all succeeding taxable years.

(2)REVOCATION

An election under subsection (c)(1) made by a corporation, trust, or association may be revoked by it for any taxable year after the first taxable year for which the election is effective. A revocation under this paragraph shall be effective for the taxable year in which made and for all succeeding taxable years. Such revocation must be made on or before the 90th day after the first day of the first taxable year for which the revocation is to be effective. Such revocation shall be made in such manner as the Secretary shall prescribe by regulations.

(3)ELECTION AFTER TERMINATION OR REVOCATION

Except as provided in paragraph (4), if a corporation, trust, or association has made an election under subsection (c)(1) and such election has been terminated or revoked under paragraph (1) or paragraph (2), such corporation, trust, or association (and any successor corporation, trust, or association) shall not be eligible to make an election under subsection (c)(1) for any taxable year prior to the fifth taxable year which begins after the first taxable year for which such termination or revocation is effective.

(4)EXCEPTIONIf the election of a corporation, trust, or association has been

terminated under paragraph (1), paragraph (3) shall not apply if—

(A)the corporation, trust, or association does not willfully fail to file within the time prescribed by law an income tax return for the taxable year with respect to which the termination of the election under subsection (c)(1) occurs;

(B)the inclusion of any incorrect information in the return referred to in subparagraph (A) is not due to fraud with intent to evade tax; and

(C)the corporation, trust, or association establishes to the satisfaction of the Secretary that its failure to qualify as a real estate investment trust to which the provisions of this part apply is due to reasonable cause and not due to willful neglect.

(5) ENTITIES TO WHICH PARAGRAPH APPLIES This paragraph applies to a corporation, trust, or association—

(A)which is not a real estate investment trust to which the provisions of this part apply for the taxable year due to one or more failures to comply with one or more of the provisions of this part (other than paragraph (2), (3), or (4) of subsection (c)),

(B)such failures are due to reasonable cause and not due to willful neglect, and

(C)if such corporation, trust, or association pays (as prescribed by the Secretary in regulations and in the same manner as tax) a penalty of \$50,000 for each failure to satisfy a provision of this part due to reasonable cause and not willful neglect.

(h) CLOSELY HELD DETERMINATIONS

(1) SECTION 542(A)(2) APPLIED

(A) In general

For purposes of subsection (a)(6), a corporation, trust, or association is closely held if the stock ownership requirement of section 542(a)(2) is met.

(B) Waiver of partnership attribution, etc. For purposes of subparagraph (A)—

(i) paragraph (2) of section 544(a) shall be applied as if such paragraph did not contain the phrase “or by or for his partner”, and

(ii) sections 544(a)(4)(A) and 544(b)(1) shall be applied by substituting “the entity meet the stock ownership requirement of section 542(a)(2)” for “the corporation a personal holding company”.

(2) SUBSECTIONS (A)(5) AND (6) NOT TO APPLY TO 1ST YEAR

Paragraphs (5) and (6) of subsection (a) shall not apply to the 1st taxable year for which an election is made under subsection (c)(1) by any corporation, trust, or association.

(3) TREATMENT OF TRUSTS DESCRIBED IN SECTION 401(A)**(A) Look-thru treatment****(i) In general**

Except as provided in clause (ii), in determining whether the stock ownership requirement of section 542(a)(2) is met for purposes of paragraph (1)(A), any stock held by a qualified trust shall be treated as held directly by its beneficiaries in proportion to their actuarial interests in such trust and shall not be treated as held by such trust.

(ii) Certain related trusts not eligible

Clause (i) shall not apply to any qualified trust if one or more disqualified persons (as defined in section 4975(e)(2), without regard to subparagraphs (B) and (I) thereof) with respect to such qualified trust hold in the aggregate 5 percent or more in value of the interests in the real estate investment trust and such real estate investment trust has accumulated earnings and profits attributable to any period for which it did not qualify as a real estate investment trust.

(B) Coordination with personal holding company rules

If any entity qualifies as a real estate investment trust for any taxable year by reason of subparagraph (A), such entity shall not be treated as a personal holding company for such taxable year for purposes of part II of subchapter G of this chapter.

(C) Treatment for purposes of unrelated business tax If any qualified trust holds more than 10 percent (by value) of the interests in any pension-held REIT at any time during a taxable year, the trust shall be treated as having for such taxable year gross income from an unrelated trade or business in an amount which bears the same ratio to the aggregate dividends paid (or treated as paid) by the REIT to the trust for the taxable year of the REIT with or within which the taxable year of the trust ends (the "REIT year") as—

(i) the gross income (less direct expenses related thereto) of the REIT for the REIT year from unrelated trades or businesses (determined as if the REIT were a qualified trust), bears to

(ii) the gross income (less direct expenses related thereto) of the REIT for the REIT year.

This subparagraph shall apply only if the ratio determined under the preceding sentence is at least 5 percent.

(D) Pension-held REIT The purposes of subparagraph (C)—

(i) In general

A real estate investment trust is a pension-held REIT if such trust would not have qualified as a real estate investment trust but for the provisions of this paragraph and if such trust is predominantly held by qualified trusts.

(ii) Predominantly held For purposes of clause (i), a real estate investment trust is predominantly held by qualified trusts if—

(I) at least 1 qualified trust holds more than 25 percent (by value) of the interests in such real estate investment trust, or

(II) 1 or more qualified trusts (each of whom own more than 10 percent by value of the interests in such real estate investment trust) hold in the aggregate more than 50 percent (by value) of the interests in such real estate investment trust.

(E) Qualified trust

For purposes of this paragraph, the term “qualified trust” means any trust described in section 401(a) and exempt from tax under section 501(a).

(i) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES

(1) IN GENERAL For purposes of this title—

(A) a corporation which is a qualified REIT subsidiary shall not be treated as a separate corporation, and

(B) all assets, liabilities, and items of income, deduction, and credit of a qualified REIT subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the real estate investment trust.

(2) QUALIFIED REIT SUBSIDIARY

For purposes of this subsection, the term “qualified REIT subsidiary” means any corporation if 100 percent of the stock of such corporation is held by the real estate investment trust. Such term shall not include a taxable REIT subsidiary.

(3) TREATMENT OF TERMINATION OF QUALIFIED SUBSIDIARY STATUS

For purposes of this subtitle, if any corporation which was a qualified REIT subsidiary ceases to meet the requirements of paragraph (2), such corporation

shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the real estate investment trust in exchange for its stock.

(j) TREATMENT OF SHARED APPRECIATION MORTGAGES

(1) IN GENERAL

Solely for purposes of subsection (c) of this section and section 857(b)(6), any income derived from a shared appreciation provision shall be treated as gain recognized on the sale of the secured property.

(2) TREATMENT OF INCOME For purposes of applying subsection (c) of this section and section 857(b)(6) to any income described in paragraph (1)—

(A) the real estate investment trust shall be treated as holding the secured property for the period during which it held the shared appreciation provision (or, if shorter, for the period during which the secured property was held by the person holding such property), and

(B) the secured property shall be treated as property described in section 1221(a)(1) if it is so described in the hands of the person holding the secured property (or it would be so described if held by the real estate investment trust).

(3) COORDINATION WITH PROHIBITED TRANSACTIONS SAFE HARBOR For purposes of section 857(b)(6)(C)—

(A) the real estate investment trust shall be treated as having sold the secured property when it recognizes any income described in paragraph (1), and

(B) any expenditures made by any holder of the secured property shall be treated as made by the real estate investment trust.

(4) COORDINATION WITH 4-YEAR HOLDING PERIOD

(A) In general For purposes of section 857(b)(6)(C), if a real estate investment trust is treated as having sold secured property under paragraph (3)(A), the trust shall be treated as having held such property for at least 4 years if—

(i) the secured property is sold or otherwise disposed of pursuant to a case under title 11 of the United States Code,

(ii) the seller is under the jurisdiction of the court in such case, and

(iii) the disposition is required by the court or is pursuant to a plan approved by the court.

(B)Exception Subparagraph (A) shall not apply if—

- (i) the secured property was acquired by the seller with the intent to evict or foreclose, or
- (ii) the trust knew or had reason to know that default on the obligation described in paragraph (5)(A) would occur.

(5)DEFINITIONS For purposes of this subsection—

(A)Shared appreciation provision The term “shared appreciation provision” means any provision—

- (i) which is in connection with an obligation which is held by the real estate investment trust and is secured by an interest in real property, and
- (ii) which entitles the real estate investment trust to receive a specified portion of any gain realized on the sale or exchange of such real property (or of any gain which would be realized if the property were sold on a specified date) or appreciation in value as of any specified date.

(B)Secured property

The term “secured property” means the real property referred to in subparagraph (A).

(k)REQUIREMENT THAT ENTITY NOT BE CLOSELY HELD TREATED AS MET IN CERTAIN CASES A corporation, trust, or association—

- (1) which for a taxable year meets the requirements of section 857(f)(1), and
 - (2) which does not know, or exercising reasonable diligence would not have known, whether the entity failed to meet the requirement of subsection (a)(6),
- shall be treated as having met the requirement of subsection (a)(6) for the taxable year.

(l)TAXABLE REIT SUBSIDIARY For purposes of this part—

(1)IN GENERAL The term “taxable REIT subsidiary” means, with respect to a real estate investment trust, a corporation (other than a real estate investment trust) if—

- (A) such trust directly or indirectly owns stock in such corporation, and
- (B) such trust and such corporation jointly elect that such corporation shall be treated as a taxable REIT subsidiary of such trust for purposes of this part.

Such an election, once made, shall be irrevocable unless both such trust and corporation consent to its revocation. Such election, and any revocation thereof, may be made without the consent of the Secretary.

(2)THIRTY-FIVE PERCENT OWNERSHIP IN ANOTHER TAXABLE REIT SUBSIDIARYThe term “taxable REIT subsidiary” includes, with respect to any real estate investment trust, any corporation (other than a real estate investment trust) with respect to which a taxable REIT subsidiary of such trust owns directly or indirectly—

(A)securities possessing more than 35 percent of the total voting power of the outstanding securities of such corporation, or

(B)securities having a value of more than 35 percent of the total value of the outstanding securities of such corporation.

The preceding sentence shall not apply to a qualified REIT subsidiary (as defined in subsection (i)(2)). For purposes of subparagraph (B), securities described in subsection (m)(2)(A) shall not be taken into account.

(3)EXCEPTIONSThe term “taxable REIT subsidiary” shall not include—

(A)any corporation which directly or indirectly operates or manages a lodging facility or a health care facility, and

(B)any corporation which directly or indirectly provides to any other person (under a franchise, license, or otherwise) rights to any brand name under which any lodging facility or health care facility is operated.

Subparagraph (B) shall not apply to rights provided to an eligible independent contractor to operate or manage a lodging facility or a health care facility if such rights are held by such corporation as a franchisee, licensee, or in a similar capacity and such lodging facility or health care facility is either owned by such corporation or is leased to such corporation from the real estate investment trust.

(4)DEFINITIONSFor purposes of paragraph (3)—

(A)Lodging facility

The term “lodging facility” has the meaning given to such term by subsection (d)(9)(D)(ii).

(B)Health care facility

The term “health care facility” has the meaning given to such term by subsection (e)(6)(D)(ii).

(m)SAFE HARBOR IN APPLYING SUBSECTION (c)(4)

(1)IN GENERALIn applying subclause (III) of subsection (c)(4)(B)(iii), except as otherwise determined by the Secretary in regulations, the following shall not be considered securities held by the trust:

(A)Straight debt securities of an issuer which meet the requirements of paragraph (2).

(B)Any loan to an individual or an estate.

(C)Any section 467 rental agreement (as defined in section 467(d)), other than with a person described in subsection (d)(2)(B).

(D)Any obligation to pay rents from real property (as defined in subsection (d)(1)).

(E)Any security issued by a State or any political subdivision thereof, the District of Columbia, a foreign government or any political subdivision thereof, or the Commonwealth of Puerto Rico, but only if the determination of any payment received or accrued under such security does not depend in whole or in part on the profits of any entity not described in this subparagraph or payments on any obligation issued by such an entity,

(F)Any security issued by a real estate investment trust.

(G)Any other arrangement as determined by the Secretary.

(2)SPECIAL RULES RELATING TO STRAIGHT DEBT SECURITIES

(A)In general

For purposes of paragraph (1)(A), securities meet the requirements of this paragraph if such securities are straight debt, as defined in section 1361(c)(5) (without regard to subparagraph (B)(iii) thereof).

(B)Special rules relating to certain contingenciesFor purposes of subparagraph (A), any interest or principal shall not be treated as failing to satisfy section 1361(c)(5)(B)(i) solely by reason of the fact that—

(i)the time of payment of such interest or principal is subject to a contingency, but only if—

(I)any such contingency does not have the effect of changing the effective yield to maturity, as determined under section 1272, other than a change in the annual yield to maturity which does not exceed the greater of $\frac{1}{4}$ of 1 percent or 5 percent of the annual yield to maturity, or

(II)neither the aggregate issue price nor the aggregate face amount of the issuer's debt instruments held by the trust exceeds \$1,000,000 and not more than 12 months of unaccrued interest can be required to

be prepaid thereunder, or

(ii) the time or amount of payment is subject to a contingency upon a default or the exercise of a prepayment right by the issuer of the debt, but only if such contingency is consistent with customary commercial practice.

(C) Special rules relating to corporate or partnership issuers In the case of an issuer which is a corporation or a partnership, securities that otherwise would be described in paragraph (1)(A) shall be considered not to be so described if the trust holding such securities and any of its controlled taxable REIT subsidiaries (as defined in subsection (d)(8)(A)(iv)) hold any securities of the issuer which—

(i) are not described in paragraph (1) (prior to the application of this subparagraph), and

(ii) have an aggregate value greater than 1 percent of the issuer's outstanding securities determined without regard to paragraph (3)(A)(i).

(3) LOOK-THROUGH RULE FOR PARTNERSHIP SECURITIES

(A) In general For purposes of applying subclause (III) of subsection (c)(4)(B)(iii)—

(i) a trust's interest as a partner in a partnership (as defined in section 7701(a)(2)) shall not be considered a security, and

(ii) the trust shall be deemed to own its proportionate share of each of the assets of the partnership.

(B) Determination of trust's interest in partnership assets For purposes of subparagraph (A), with respect to any taxable year beginning after the date of the enactment of this subparagraph—

(i) the trust's interest in the partnership assets shall be the trust's proportionate interest in any securities issued by the partnership (determined without regard to subparagraph (A)(i) and paragraph (4), but not including securities described in paragraph (1)), and

(ii) the value of any debt instrument shall be the adjusted issue price thereof, as defined in section 1272(a)(4).

(4) CERTAIN PARTNERSHIP DEBT INSTRUMENTS NOT TREATED AS A SECURITY For purposes of applying subclause (III) of subsection (c)(4)(B)(iii)—

(A) any debt instrument issued by a partnership and not described in

paragraph (1) shall not be considered a security to the extent of the trust's interest as a partner in the partnership, and

(B)any debt instrument issued by a partnership and not described in paragraph (1) shall not be considered a security if at least 75 percent of the partnership's gross income (excluding gross income from prohibited transactions) is derived from sources referred to in subsection (c)(3).

(5) SECRETARIAL GUIDANCE

The Secretary is authorized to provide guidance (including through the issuance of a written determination, as defined in section 6110(b)) that an arrangement shall not be considered a security held by the trust for purposes of applying subclause (III) of subsection (c)(4)(B)(iii) notwithstanding that such arrangement otherwise could be considered a security under subparagraph (F) of subsection (c)(5).

(6) TRANSITION RULE

(A) In general Notwithstanding paragraph (2)(C), securities held by a trust shall not be considered securities held by the trust for purposes of subsection (c)(4)(B)(iii)(III) during any period beginning on or before October 22, 2004, if such securities—

(i) are held by such trust continuously during such period, and

(ii) would not be taken into account for purposes of such subsection by reason of paragraph (7)(C) of subsection (c) (as in effect on October 22, 2004) if the amendments made by section 243 of the American Jobs Creation Act of 2004 had never been enacted.

(B) Rule not to apply to securities held after maturity date

Subparagraph (A) shall not apply with respect to any security after the later of October 22, 2004, or the latest maturity date under the contract (as in effect on October 22, 2004) taking into account any renewal or extension permitted under the contract if such renewal or extension does not significantly modify any other terms of the contract.

(C) Successors

If the successor of a trust to which this paragraph applies acquires securities in a transaction to which section 381 applies, such trusts shall be treated as a single entity for purposes of determining the holding period of such securities under subparagraph (A).

(n) RULES REGARDING FOREIGN CURRENCY TRANSACTIONS

(1) In general For purposes of this part—

(A)passive foreign exchange gain for any taxable year shall not constitute gross income for purposes of subsection (c)(2), and

(B)real estate foreign exchange gain for any taxable year shall not constitute gross income for purposes of subsection (c)(3).

(2)REAL ESTATE FOREIGN EXCHANGE GAINFor purposes of this subsection, the term “real estate foreign exchange gain” means—

(A)foreign currency gain (as defined in section 988(b)(1)) which is attributable to—

(i)any item of income or gain described in subsection (c)(3),

(ii)the acquisition or ownership of obligations secured by mortgages on real property or on interests in real property (other than foreign currency gain attributable to any item of income or gain described in clause (i)), or

(iii)becoming or being the obligor under obligations secured by mortgages on real property or on interests in real property (other than foreign currency gain attributable to any item of income or gain described in clause (i)),

(B)section 987 gain attributable to a qualified business unit (as defined by section 989) of the real estate investment trust, but only if such qualified business unit meets the requirements under—

(i)subsection (c)(3) for the taxable year, and

(ii)subsection (c)(4)(A) at the close of each quarter that the real estate investment trust has directly or indirectly held the qualified business unit, and

(C)any other foreign currency gain as determined by the Secretary.

(3)PASSIVE FOREIGN EXCHANGE GAINFor purposes of this subsection, the term “passive foreign exchange gain” means—

(A)real estate foreign exchange gain,

(B)foreign currency gain (as defined in section 988(b)(1)) which is not described in subparagraph (A) and which is attributable to—

(i)any item of income or gain described in subsection (c)(2),

(ii)the acquisition or ownership of obligations (other than foreign currency gain attributable to any item of income or gain described in clause (i)), or

(iii)becoming or being the obligor under obligations (other than foreign

currency gain attributable to any item of income or gain described in clause (i)), and

(C) any other foreign currency gain as determined by the Secretary.

(4) EXCEPTION FOR INCOME FROM SUBSTANTIAL AND REGULAR TRADING

Notwithstanding this subsection or any other provision of this part, any section 988 gain derived by a corporation, trust, or association from dealing, or engaging in substantial and regular trading, in securities (as defined in section 475(c)(2)) shall constitute gross income which does not qualify under paragraph (2) or (3) of subsection (c). This paragraph shall not apply to income which does not constitute gross income by reason of subsection (c)(5)(G).

(Added [Pub. L. 86-779, § 10\(a\)](#), Sept. 14, 1960, [74 Stat. 1004](#); amended [Pub. L. 88-272, title II, § 225\(k\)\(4\)](#), Feb. 26, 1964, [78 Stat. 94](#); [Pub. L. 88-554, § 4\(b\)\(4\)](#), Aug. 31, 1964, [78 Stat. 763](#); [Pub. L. 93-625, § 6\(a\)](#), (b), (d)(1), Jan. 3, 1975, [88 Stat. 2112-2114](#); [Pub. L. 94-455, title XIV, § 1402\(b\)\(1\)\(O\)](#), (2), title XVI, §§ 1602(a), 1603(a), (c)(1)-(4), 1604(a)-(c)(1), (d)-(f)(3)(A), (g), (k)(1), (2)(A), title XIX, §§ 1901(a)(111), 1906(b)(13)(A), Oct. 4, 1976, [90 Stat. 1732](#), 1746, 1748-1753, 1783, 1834; [Pub. L. 95-600, title III, § 363\(a\)](#), (c), title VII, § 701(t)(2), Nov. 6, 1978, [92 Stat. 2852](#), 2853, 2912; [Pub. L. 98-369, div. A, title X, § 1001\(b\)\(12\)](#), (e), July 18, 1984, [98 Stat. 1011](#), 1012; [Pub. L. 99-514, title VI](#), §§ 661(a), 662, 663, 671(b)(1), title IX, § 901(d)(4) (E), Oct. 22, 1986, [100 Stat. 2299](#), 2300, 2302, 2317, 2380; [Pub. L. 100-647, title I, § 1006\(p\)\(1\)](#), (3), (4)(A), (5), (q), (t)(11), Nov. 10, 1988, [102 Stat. 3416](#), 3417, 3422; [Pub. L. 103-66, title XIII, § 13149\(a\)](#), Aug. 10, 1993, [107 Stat. 445](#); [Pub. L. 104-188, title I](#), §§ 1621(b)(5), 1704(t)(35), Aug. 20, 1996, [110 Stat. 1867](#), 1889; [Pub. L. 105-34, title XII](#), §§ 1251(b)-1253, 1255(a), (b)(1), 1257, 1258, 1261, 1262, Aug. 5, 1997, [111 Stat. 1031-1036](#); [Pub. L. 106-170, title V](#), §§ 532(c)(2)(H)-(K), 541-542(b)(3)(A)(i), (B)(i), 543, 551(a), 561(a), Dec. 17, 1999, [113 Stat. 1930](#), 1940-1943, 1948, 1949; [Pub. L. 106-554, § 1\(a\)\(7\)](#) [title III, § 319(9), (10)], Dec. 21, 2000, [114 Stat. 2763](#), 2763A-646; [Pub. L. 108-357, title II, § 243\(a\)](#), (b), (d), (f)(1)-(3), title VIII, § 835(b)(4), Oct. 22, 2004, [118 Stat. 1439](#), 1441-1444, 1593; [Pub. L. 109-135, title IV](#), §§ 403(d)(1), (2), 412(hh), Dec. 21, 2005, [119 Stat. 2620](#), 2622, 2639; [Pub. L. 110-172](#), §§ 9(b), 11(a)(18), Dec. 29, 2007, [121 Stat. 2484](#), 2486; [Pub. L. 110-234, title XV](#), §§ 15312(a), (b), 15313(a), (b), 15314(a), May 22, 2008, [122 Stat. 1503](#), 1504; [Pub. L. 110-246, § 4\(a\)](#), title XV, §§ 15312(a), (b), 15313(a), (b), 15314(a), June 18, 2008, [122 Stat. 1664](#), 2265, 2266; [Pub. L. 110-289, div. C, title II](#), §§ 3031, 3032, 3041, 3061, July 30, 2008, [122 Stat. 2897](#), 2899-2901.)

[\[1\]](#) So in original. Probably should be followed by "and".