

26 CFR 601.601. Rules and regulations.
(Also Part I, §163(j).)

Rev. Proc. 2021-9

SECTION 1. PURPOSE

This revenue procedure provides a safe harbor that allows a trade or business that manages or operates a qualified residential living facility, as defined in section 3.01 of this revenue procedure, to be treated as a real property trade or business, solely for purposes of qualifying to make the election under section 163(j)(7)(B) of the Internal Revenue Code (Code) to be an electing real property trade or business.

SECTION 2. BACKGROUND

.01 On December 22, 2017, section 163(j) was amended by § 13301 of Public Law No. 115-97, 131 Stat. 2054, commonly referred to as the Tax Cuts and Jobs Act (TCJA). Section 163(j), as amended by the TCJA, provides rules limiting the amount of business interest expense that can be deducted for taxable years beginning after December 31, 2017. See TCJA § 13301(a).

.02 On March 27, 2020, section 163(j) was further amended by § 2306 of the Coronavirus Aid, Relief, and Economic Security Act, Public Law No. 116-136, 13 Stat. 281 (CARES Act), to provide special rules for applying section 163(j) to taxable years

beginning in 2019 or 2020.

.03 Under section 163(j)(1), the amount allowed as a deduction for business interest expense is limited to the sum of: (1) the taxpayer's business interest income, as defined in section 163(j)(6), for the taxable year; (2) 30 percent of the taxpayer's adjusted taxable income, as defined in section 163(j)(8), for such taxable year, or 50 percent of the taxpayer's adjusted taxable income (if applicable, as provided in section 163(j)(10)); and (3) the taxpayer's floor plan financing interest, as defined in section 163(j)(9), for such taxable year.

.04 The limitation under section 163(j) on the deductibility of business interest expense applies to all taxpayers with business interest, as defined in section 163(j)(5), except for taxpayers, other than tax shelters under section 448(a)(3), that meet the gross receipts test in section 448(c).

.05 Section 163(j)(5) generally provides that the term "business interest" means any interest expense properly allocable to a trade or business. Section 163(j)(7)(A)(ii) provides that, for purposes of the limitation on the deduction for business interest, the term "trade or business" does not include an "electing real property trade or business." Thus, interest expense properly allocable to an electing real property trade or business is not properly allocable to a trade or business for purposes of section 163(j), and is not business interest expense that is subject to section 163(j)(1).

.06 The term "electing real property trade or business" under section 163(j)(7)(B) means "any trade or business which is described in section 469(c)(7)(C) and which makes an election" to be an electing real property trade or business.

.07 Section 168(g)(1)(F) provides that an electing real property trade or business

within the meaning of section 163(j)(7)(B) must use the alternative depreciation system for property described in section 168(g)(8). See section 163(j)(11)(A).

.08 The Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) published (1) proposed regulations under section 163(j) in a notice of proposed rulemaking (REG-106089-18) in the Federal Register (83 FR 67490) on December 28, 2018 (2018 proposed regulations), (2) final regulations under section 163(j) (TD 9905) in the Federal Register (85 FR 56686) on September 14, 2020 (final regulations), and (3) concurrently with the publication of the final regulations, additional proposed regulations under section 163(j) in a notice of proposed rulemaking (REG-107911-18) in the Federal Register (85 FR 56846).

.09 Section 1.163(j)-1(b)(14) of the final regulations defines an electing real property trade or business as one that makes an election under § 1.163(j)-9 or other published guidance that is (1) a real property trade or business described in section 469(c)(7)(C) of the Code and § 1.469-9(b)(2) of the final regulations, (2) a REIT that qualifies for the safe harbor described in § 1.163(j)-9(h), or (3) a trade or business specifically designated by the Secretary of the Treasury or his delegate in guidance published in the Federal Register or the Internal Revenue Bulletin as a real property trade or business for section 163(j).

.10 Section 1.163(j)-9 provides rules and procedures for making an election under section 163(j)(7)(B) to be an electing real property trade or business. The Treasury Department and the IRS released Rev. Proc. 2020-22, 2020-18 I.R.B. 745, (April 27, 2020) to provide the time and manner of making a late election, or withdrawing an election under section 163(j)(7)(B) to be an electing real property trade or business for

taxable years beginning in 2018, 2019, or 2020. Rev. Proc. 2020-22 also provides the time and manner of making or revoking elections provided by the CARES Act under section 163(j)(10) for taxable years beginning in 2019 or 2020. See Rev. Proc. 2020-22 for more information regarding the time and manner of making, revoking, or withdrawing elections under section 163(j)(7) and (10).

.11 Section 469(c)(7)(C) defines a real property trade or business as any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business. See also § 1.469-9(b)(2).

.12 In response to the 2018 proposed regulations, commenters expressed concern as to whether a trade or business that manages or operates a residential living facility and also provides supplemental assistive, nursing, or routine medical services to its customers or patients is eligible to make the election under section 163(j)(7)(B) to be an electing real property trade or business.

.13 On September 28, 2020, the Treasury Department and the IRS published Notice 2020-59, 2020-40 I.R.B. 782, which contained a proposed revenue procedure providing a safe harbor for a trade or business that manages or operates a qualified residential living facility, as defined in section 3.01 of the proposed revenue procedure, to be treated as a real property trade or business solely for purposes of qualifying to make the election under section 163(j)(7)(B) to be treated as an electing real property trade or business. Notice 2020-59 requested comments on the proposed revenue procedure.

.14 In response to the proposed revenue procedure in Notice 2020-59, commenters presented three distinct concerns:

(1) First, commenters requested that the definition of a qualified residential living facility be modified to reduce the minimum threshold for the average period of customer or patient use of individual dwelling units requirement from 90 days to less than 90 days, and that the determination of the average period of customer or patient use take into account that some customers or patients may reside at the facility without a rental contract or other formal written lease agreement. Because Medicare and Medicaid plans generally pay for stays that are substantially less than 90 days, commenters noted that the 90-day average period of customer or patient use requirement would unfairly penalize taxpayers with large numbers of Medicare and Medicaid patients and potentially exclude taxpayers that Congress intended to be eligible to make a real property trade or business election under section 163(j)(7)(B). Commenters also explicitly mentioned that certain facilities that are wholly or partially licensed to receive Medicare and Medicaid payments provide care outside of a rental contract or other formal written lease agreement. The Treasury Department and the IRS agree with this comment, and accordingly, this revenue procedure reduces the average period for customer or patient use requirement from 90 days to 30 days, and allows taxpayers to determine the average period by reference to either the number of days paid for by Medicare or Medicaid or the number of days under a rental contract or other formal written lease agreement.

(2) Second, commenters requested that the revenue procedure provide an alternative test to meet certain requirements of the definition of a qualified residential living facility. Commenters specifically proposed using the definition of “residential rental property” under section 168(e)(2)(A) of the Code as an alternative to the requirements in

section 3.01(1) (primary residence requirement) and 3.01(3) (average period of customer or patient use requirement) of the proposed revenue procedure, in part because the legislative history of the TCJA confirms that the trade or business of operating or managing “residential rental property” housing the elderly is eligible to be a real property trade or business despite the provision of necessary supplemental assistive services to the residents of the residential rental property. Moreover, commenters pointed out the linkage between section 168 and section 163(j) because section 168(g)(1)(F) provides that an electing real property trade or business within the meaning of section 163(j)(7)(B) must use the alternative depreciation system for property described in section 168(g)(8), which includes residential rental property, and because the IRS has previously concluded that various types of retirement care facilities, including independent living, assisted living, and skilled nursing facilities, for example, may qualify as residential rental property for purposes of section 168(e)(2)(A). Commenters also noted that taxpayers have to determine whether their facilities qualify as residential rental property under section 168(e)(2)(A) for purposes of calculating depreciation. They indicated that allowing the section 168(e)(2)(A) test to be used as an alternative to the primary residence requirement and the average period of customer or patient use requirement would reduce taxpayer burden. The Treasury Department and the IRS agree with this comment and this revenue procedure includes an alternative test providing that if a taxpayer operates or manages residential living facilities that qualify as residential rental property under section 168(e)(2)(A), then the facility also meets the requirements set forth in section 3.01(1) and (3) of this revenue procedure.

(3) Third, commenters requested clarification on whether a taxpayer’s reliance on

the residential living facility safe harbor to make an election under section 163(j)(7)(B) to be an electing real property trade or business must be determined on an annual basis or remains in effect for taxable years after the taxable year in which an initial election is made. Generally, taxpayers may make an irrevocable one-time election under section 163(j)(7)(B) and § 1.163(j)-9(c) to be an electing real property trade or business. This election, once made, applies to the taxable year in which the election is made and to all subsequent taxable years, and automatically terminates under § 1.163(j)-9(e)(1) if the taxpayer ceases to engage in the electing trade or business. Thus, commenters requested that the proposed revenue procedure be amended to clarify that the same rules apply to a taxpayer relying on the safe harbor to make the election such that a trade or business may make a one-time determination as to whether it qualifies for the safe harbor. The Treasury Department and the IRS decline to adopt this comment. An annual test is necessary under the safe harbor because, unlike most trades or businesses that are subject to the electing real property trade or business provisions in § 1.163(j)-9, taxpayers relying solely on the safe harbor provided in this revenue procedure must perform a mathematical calculation to determine their eligibility to make the real property trade or business election under 163(j)(7)(B), and eligibility is conditioned upon continuing to meet the eligibility requirements for each taxable year. This revenue procedure clarifies that, if the taxpayer fails to satisfy the requirements to be a qualified residential living facility in section 3.01 of this revenue procedure in a subsequent taxable year, the residential living facility safe harbor no longer applies and the taxpayer is deemed to have ceased the electing trade or business. This deemed cessation of the electing trade or business does not apply to taxpayers that otherwise

continue to qualify as an electing real property trade or business without the use of the safe harbor. If, in a taxable year subsequent to the taxable year in which the taxpayer is deemed to have ceased the electing trade or business the taxpayer again satisfies the requirements in section 3.01 of this revenue procedure, the taxpayer's initial election pursuant to the residential living facility safe harbor will be automatically reinstated. See § 1.168(i)-4(d) and section 4.02 of Rev. Proc. 2019-08, 2019-03 I.R.B. 347 (January 14, 2019) for guidance on how to change the computation of depreciation for certain property held by an electing real property trade or business.

.15 In light of the comments received in response to the 2018 proposed regulations and to Notice 2020-59, this revenue procedure provides a safe harbor that allows a taxpayer engaged in a trade or business that manages or operates a qualified residential living facility, as defined in section 3.01 of this revenue procedure, to treat the trade or business as a real property trade or business solely for purposes of qualifying to make an election under section 163(j)(7)(B) to be an electing real property trade or business (residential living facility safe harbor).

SECTION 3. DEFINITIONS FOR RESIDENTIAL LIVING FACILITY SAFE HARBOR

The following definitions apply for purposes of this revenue procedure:

.01 Qualified Residential Living Facility. Except as provided in sections 3.02 and 4.04 of this revenue procedure, a "qualified residential living facility" is a residential living facility that:

(1) Consists of multiple rental dwelling units within one or more buildings or structures that generally serve as primary residences on a permanent or semi-permanent basis to individual customers or patients;

(2) Provides supplemental assistive, nursing, or other routine medical services;
and

(3) Has an average period of customer or patient use of individual rental dwelling units of 30 days or more.

.02 Section 168(e)(2)(A) test. A residential living facility that qualifies as residential rental property under section 168(e)(2)(A) satisfies the requirements in section 3.01(1) and (3) of this revenue procedure.

.03 Average period of customer or patient use.

(1) In general. The “average period of customer or patient use” is determined by dividing: (i) the sum of the total number of days in the taxable year that each customer or patient resides in a rental dwelling unit of the residential living facility, which may be determined by reference to a rental contract or other formal written lease agreement, or by the number of days paid for by Medicare or Medicaid; by (ii) the total number of individual residential customers or patients that reside in all of the rental dwelling units of the facility for the taxable year. For this purpose, a married couple residing in a single rental dwelling unit of the residential living facility will be counted as one individual customer or patient, unless each spouse is separately properly treated as an individual customer or patient of the residential living facility that receives supplemental assistive, nursing, or other routine medical services from or on behalf of the residential living facility. Days in which a rental dwelling unit of a residential living facility are not occupied are not included in the calculation of the average period of customer or patient use.

(2) Example. Facility has 100 rental dwelling units. Of the 100 units, 60 units are

occupied by the same customer or patient for the entire year, 25 other units are occupied for 360 days of the year with each customer or patient occupying a unit for 90 days, and the remaining 15 units are occupied for a total of 10 months (March through December = 306 days) of the year. Of the 15 units occupied for 10 months of the year, 10 units are occupied by customers or patients during the entire months of March through July (153 days) and by different customers or patients during the entire months of August through December (153 days), for a total of 20 customers for the 10-month period. For the remaining 5 of the 15 units that are occupied for 10 months of the year, 5 customers or patients occupy the units for 8 months (May through December = 245 days) of the year, and 5 other customers or patients occupy the units for 2 months (September and October = 61 days) of the year. The average period of customer or patient use is determined by dividing the sum of the total number of days in the taxable year that each customer resides in a rental dwelling unit, by the total number of individual residential customers or patients that reside in all of the rental dwelling units for the taxable year. The total number of days in the taxable year that the customers or patients reside in the rental dwelling unit is 35,490 days [21,900 days (60 units that are occupied for the entire year x 365 days per year) + 9,000 days (25 units that are occupied for 90 days each x 90 days x 4 90-day periods) + 4,590 days (15 units that are occupied for 10 months x 306 days)]. The total number of individual residential customers or patients is 190 [60 customers or patients occupying a unit for the entire year + 100 (25 customers or patients occupying units for 90 days each x 4 90-day periods in a year) + 20 customers or patients that occupy a unit for a 5-month period + 5 customers or patients that occupy a unit for a 8-month period + 5 customers or patients

that occupy a unit for a 2-month period]. Accordingly, the average period of customer or patient use is approximately 187 days (35,490/190).

.04 Supplemental assistive, nursing, or other routine medical services.

“Supplemental assistive, nursing, or other routine medical services” are personal and professional services that are customarily and routinely provided to individual residential customers or patients of nursing homes, assisted living facilities, memory care residences, continuing care retirement communities, skilled nursing facilities, or similar facilities, as needed, on a day-to-day basis. Such services generally do not include surgical, radiological, or other intensive or specialized medical services that are usually provided only in emergency or short-term in-patient or out-patient hospital or surgical settings.

.05 Permanent or semi-permanent basis. The rental dwelling units of a residential living facility serve as primary residences on a “permanent or semi-permanent basis” to customers or patients whose use of the units is generally long-term (30 days or more) in nature, even though some customers or patients may arrive at the residential living facility with significantly shortened life expectancies due to advanced age or terminal medical conditions, and some customers or patients otherwise may be expected to periodically reside away from the residential living facility, such as at the primary residence of a spouse or other relative, for short periods of time.

SECTION 4. RESIDENTIAL LIVING FACILITY SAFE HARBOR

.01 Safe harbor for residential living facility trades or businesses. A taxpayer engaged in a trade or business that manages or operates a qualified residential living facility, as defined in section 3.01 of this revenue procedure, may treat such trade or

business as a real property trade or business solely for purposes of the election under section 163(j)(7)(B) to be an electing real property trade or business. Satisfying the requirements of this safe harbor is not a determination that the taxpayer is engaged in a real property trade or business under section 469.

.02 Effect of election and how to make the election. If a taxpayer relies on this safe harbor in section 4.01 this revenue procedure to make the election under section 163(j)(7)(B) to be an electing real property trade or business, the provisions in § 1.163(j)-9 apply, and the taxpayer must use the alternative depreciation system of section 168(g) to depreciate the property described in section 168(g)(8). The taxpayer makes the election under section 163(j)(7)(B) at the time, and in the manner prescribed by § 1.163(j)-9(d). See also Rev. Proc. 2020-22.

.03 Substantiation. A trade or business that manages or operates a residential living facility to which this revenue procedure applies must retain books and records to substantiate that all the requirements of this section 4 have been met in accordance with section 6001.

.04 Annual test; reinstated election. For any taxable year, subsequent to the taxable year in which a taxpayer relies on the safe harbor in section 4.01 of this revenue procedure to make the election under section 163(j)(7)(B) to be treated as a real property trade or business, in which a taxpayer does not satisfy the requirements in section 3.01 of this revenue procedure, the taxpayer is deemed to have ceased to engage in the electing trade or business, as provided in § 1.163(j)-9(e) for such subsequent taxable year. For any subsequent taxable year in which a taxpayer satisfies the requirements in section 3.01 of this revenue procedure after a deemed cessation of

the electing trade or business, the taxpayer's initial election under section 163(j)(7)(B) will be automatically reinstated.

.05 Anti-abuse. Taxpayers are not eligible to rely on the safe harbor in this revenue procedure if a principal purpose of an arrangement or transaction is to avoid section 163(j) and its regulations and in a manner that is contrary to the purpose of this revenue procedure. See §1.163(j)-2(j).

SECTION 5. APPLICABILITY

Taxpayers may apply the rules of this revenue procedure to taxable years beginning after December 31, 2017.

SECTION 6. PAPERWORK REDUCTION ACT

.01 This revenue procedure does not impose any additional information collection requirements in the form of reporting, recordkeeping requirements, or third-party disclosure requirements to the burden that is accounted for in the final regulations. However, this revenue procedure provides that qualified residential living facilities, as defined in section 3.01 of this revenue procedure, may be treated as real property trades or businesses, within the meaning of section 469(c)(7)(C), solely for purposes of making the election under section 163(j)(7)(B) to qualify as an electing real property trade or business. Taxpayers relying on the safe harbor in section 4.01 of this revenue procedure must file a statement with their return under the procedures set forth in, and containing the information required by, §1.163(j)-9 and Rev. Proc. 2020-22, if applicable. That collection of information has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-0123.

.02 This information is required to be collected and retained for compliance purposes, namely, to determine whether the taxpayer has made an election for one of its trades or businesses to be an electing real property trade or business.

.03 The Treasury Department and the IRS estimate that approximately 30,210 respondents are likely. This number was determined by examining, for the 2017 tax year, Form 1120, Form 1120-S, Form 1065, and Form 1120-REIT filers with NAICS codes of 623110 (nursing care facilities (skilled nursing facilities)), 623311 (continuing care retirement communities), 623312 (assisted living facilities for the elderly) and 623990 (other residential care facilities) with gross receipts of at least \$10 million.

.04 The estimated number of respondents is 30,210. The estimated annual burden per respondent/recordkeeper varies from 0 to 30 minutes, depending on individual circumstances, with an estimated average of 15 minutes. The estimated total annual reporting and/or recordkeeping burden is 7,552.5 hours (30,210 respondents x 15 minutes). The estimated annual cost burden to respondents is \$95 per hour. Accordingly, we expect the total annual cost burden for the election statements to be \$717,487.50 (30,210 * .25 * \$95). The estimated annual frequency of responses is once because the statements only have to be filed once.

SECTION 7. DRAFTING INFORMATION

The principal authors of this revenue procedure are Susie Bird, Charles Gorham, Justin Grill, Bernard Harvey and Jaime Park of the Office of Associate Chief Counsel (Income Tax & Accounting) and Adrienne Mikolashek and William Kostak of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Mr. Grill at (202) 317-7003, or Mr.

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