

Prop. Reg. Section 1.280A-1(e)(7), Example 4

Limitations on deductions with respect to a dwelling unit which is used by the taxpayer during the taxable year as a residence.

(e) Personal use of dwelling unit--

(1) General rule.

For purposes of this section and Sections 1.280A-2 and 1.280A-3, a taxpayer shall be deemed to have used a dwelling unit for personal purposes on any day on which, for any part of the day, any portion of the unit is used--

- (i) For personal purposes by the taxpayer or any other person who has an interest in the unit;
- (ii) By a brother or sister (whether by the whole or half blood), spouse, ancestor, or lineal descendant of the taxpayer or of any other person who has an interest in the unit;
- (iii) By any individual who uses the unit under an arrangement which enables the taxpayer to use some other dwelling unit for any period of time, whether or not a rental is charged for the use of the other unit and regardless of the length of time that the taxpayer uses the other unit; or
- (iv) By any individual, other than an employee with respect to whose use section 119 (relating to meals or lodging furnished for the convenience of the employer) applies, unless for such day the dwelling unit is rented for a rental which, under the facts and circumstances, is fair rental.

For purposes of this paragraph, a person is considered to have an interest in a dwelling unit if that person holds any interest in the unit (other than a security interest or an interest under a lease for a fair rental) even if there are no immediate rights to possession and enjoyment under the interest.

(2) Rental at fair rental to other persons for use as principal residence.

Notwithstanding paragraph (e)(1) of this section, a taxpayer shall not be treated as using a dwelling unit for personal purposes by reason of a rental arrangement for any day on which the taxpayer rents the dwelling unit at a fair rental to any person for use as that person's principal residence. If a taxpayer actually makes personal use of a unit on any such day, however, that personal use is taken into account because it arises other than "by reason of a rental arrangement." For purposes of the preceding sentence, a brief visit during which the taxpayer is a guest of the occupant of the unit shall not be considered personal use by the taxpayer. For the meaning of the term "principal residence," see section 1034 and Section 1.1034-1(c)(3).

(3) Rental to persons having interest in the unit--

(i) In general.

Paragraph (e)(2) of this section shall apply in the case of a rental of a unit to a person who has an interest in the unit only if the rental is pursuant to a shared equity financing agreement.

(ii) Shared equity financing agreement.

A shared equity financing agreement is any written agreement under which--

(A) Two or more persons acquire qualified ownership interests in the dwelling unit, and

(B) A person (or persons) holding one or more of the interests is--

(1) Entitled to occupy the dwelling unit for use as a principal residence, and

(2) Required to pay rent to one or more persons holding a qualified ownership interest in the unit.

(iii) Fair rental.

For purposes of this paragraph (e)(3), the determination whether a unit is rented at a fair rental (within the meaning of paragraph (g) of this section) shall be made in light of all the facts and circumstances that existed at the time the agreement was entered into. The totality of rights and obligations of all parties under the agreement is taken into account in determining fair rental.

(iv) Qualified ownership interest.

For purposes of this paragraph (e)(3), the term "qualified ownership interest" means an undivided interest for more than 50 years in the entire dwelling unit and appurtenant land being acquired in the transaction to which the share equity financing agreement relates.

(v) Not necessary that all owners charge fair rental.

A shared equity financing arrangement may exist even if one or more of the owners does not charge the occupant fair rental for use of the unit. Paragraph (e)(2) of this section, however, applies only to those owners who do charge fair rental.

(4) Special rule for "qualified rental period."

For purposes of determining whether section 280A(c)(5) and Section 1.280A-3(d) limit deductions for expenses allocable to a "qualified rental period," a taxpayer shall not be considered to have used the rented unit for personal purposes on any day during the taxable year before or after a "qualified rental period" described in paragraph (e)(4)(i) of this section, or before a "qualified rental period" described in paragraph (e)(4)(ii) of this section, if the rented unit was the principal residence of the taxpayer with respect to that day. The use of the unit for personal purposes shall, however, be taken into account for all other purposes of section 280A. A "qualified rental period" is a consecutive period of--

(i) 12 or more months which begins or ends during the taxable year, or

(ii) less than 12 months which begins in the taxable year and at the end of which the rented unit is sold or exchanged, and for which the unit is rented, or is held for rental, at a fair rental. For the meaning of the term "principal residence," see section 1034 and Section 1.1034-1(c)(3).

(5) Dwelling units in which a partnership, a trust, an estate, or an electing small business corporation has an interest--

(i) In general.

This paragraph (e)(5) sets out special rules for purposes of applying paragraph (e)(1) and (2) of this section to a dwelling unit in which a partnership, a trust, an estate, an electing small business corporation (as defined in section 1371(b), as it read before the enactment of the Subchapter S Revision Act of 1982 [Pub. L. 97-354, 1982-2 C.B. 702]), or an S corporation (as defined in section 1361(a)) has an interest. For purposes of this paragraph (e)(5), these entities shall be referred to as pass-through entities, and any partner, beneficiary, or shareholder that owns an interest in such an entity shall be referred to as a beneficial owner of the entity.

(ii) Personal use under paragraph (e)(1).

For purposes of paragraph (e)(1) of this section, a pass-through entity shall be considered to have made personal use of a dwelling unit on any day on which any beneficial owner of the entity would be considered to have made personal use of the unit. Personal use under the preceding sentence shall be determined as if each beneficial owner had an interest in the unit. Thus, for example, personal use by a sister of a partner is considered personal use by the partnership.

(iii) Personal use under paragraph (e)(2)--

(A) In general.

For purposes of applying the second sentence of paragraph (e)(2) of this section to a dwelling unit in which a pass-through entity has an interest, actual personal use by any beneficial owner of that pass-through entity shall be treated as personal use by the entity. Deemed personal use by a beneficial owner under paragraph (e)(1), for example, by reason of the personal use of the unit by a sister of the beneficial owner, shall not be treated as personal use by the entity.

(B) Exception for certain partnerships.

If--

(1) A partnership owns an interest in a dwelling unit,

(2) A partner rents the unit from the partnership at a fair rental for use as the partner's principal residence, and

(3) The items of income, gain, loss, deduction or credit of the partnership related to the unit are allocated among the partners in accordance with their percentage ownership interest in the partnership, use of the unit by that partner as that partner's principal residence shall not be treated as personal use of the unit by the partnership for purposes of paragraph (e)(2). The partner actually making use of the unit, however, is subject to the limitations of section 280A(c)(5) with respect to items related to the unit that are allocated to that partner.

(C) Example.

The provisions of paragraph (e)(5)(iii)(B) of this section may be illustrated by the following example.

Example.

A, B, and C form partnership P, in which each holds a one-third interest. P acquires a dwelling unit that C rents from P at fair rental for use as C's principal residence. All items of income, gain, loss, deduction, or credit of P that are related to the unit are allocated one-third to each partner. Under these circumstances, the personal use of the unit by C is not treated as personal use by P. Consequently, the use of the unit by C does not subject A and B to the limitations of section 280A(c)(5) with respect to their shares of the items related to the unit. C, however, is subject to the limitations of section 280A(c)(5) with respect to C's share of those items.

(6) Use of the unit for repairs and maintenance.

Notwithstanding the provisions of paragraph (e)(1) of this section, a dwelling unit shall not be deemed to have been used by the taxpayer for personal purposes on any day on which the principal purpose of the use of the unit is to perform repair or maintenance work on the unit. Whether the principal purpose of the use of the unit is to perform repair or maintenance work shall be determined in light of all the facts and circumstances including, but not limited to, the following: the amount of time devoted to repair and maintenance work, the frequency of the use for repair and maintenance purposes during a taxable year, and the presence and activities of companions. In no case, however, shall a day on which the taxpayer engages in repair and maintenance of the unit on a substantially full-time basis be considered

a day of personal use by the taxpayer.

(7) Examples.

The provisions of this paragraph (e) may be illustrated by the following examples:

Example (1).

B owns a vacation home which B rents to S, B's sister, at fair rental for 10 days. B also rents the home to C at fair rental for 11 days as a part of an arrangement whereby B is entitled to use D's home for 6 days. As a favor, B rents the home to F at a discount rate for 15 days. On the basis of the rental activity described, B is deemed to have used the home for personal purposes for 36 days.

Example (2).

X Inc., an electing small business corporation in which A and B are shareholders, is the owner of a fully equipped recreational vehicle. During the month of July, the vehicle is used by three individuals. A uses the vehicle on a 7-day camping trip. D, who is B's daughter, rents the vehicle from X Inc. at fair rental for 10 days. E rents the vehicle at fair rental for 12 days under an arrangement whereby B is entitled to use an apartment owned by F, a friend of E, for 9 days. X Inc. is deemed to have used the dwelling unit for personal purposes on any day on which any of its shareholders would be deemed to have so used the unit. Therefore, X Inc. is deemed to have used the recreational vehicle for personal purposes on 29 days. >

Example (3).

A owns a lakeside cottage which A rents during the summer. A and B, A's spouse, arrive late Thursday evening after a long drive to prepare the cottage for the rental season. A and B prepare dinner but do no work on the unit that evening. A spends a normal work day working on the unit on Friday and Saturday; B helps for a few hours each day but spends most of the time relaxing. By Saturday evening, the necessary maintenance work is complete. Neither A nor B works on the unit on Sunday; they depart shortly before noon. The principal purpose of the use of the unit from Thursday evening through Sunday morning is to perform maintenance work on the unit. Consequently, the use during this period will not be considered personal use by A.



Example (4).

C owns a mountain cabin which C rents for most of the year. C spends a week at the cabin with family members. C works on maintenance of the cabin 3 or 4 hours each day during the week. C spends the rest of the time fishing, hiking, and relaxing. C's family members, however, work substantially full-time on the cabin on each day during the week. The principal purpose of the use of the cabin is to perform maintenance work. Therefore, the use during this period will not be considered personal use by C. >

Example (5).

B, an individual whose taxable year is the calendar year, uses a dwelling unit as a principal residence from January 1, 1978, to June 30, 1978. On July 1, 1978, B rents the unit at a fair rental to D, an unrelated individual, for a two-year period beginning immediately. In determining whether section 280A(c)(5) and Section 1.280A-3(d) limit deductions for expenses allocable to this "qualified rental period", B is not considered to have used the unit for personal purposes from January 1, 1978, to June 30, 1978. Note, however, that section 280A(e) and Section 1.280A-3(c) limit the portion of the total 1978 expenses with respect to the unit which may be attributed to the "qualified rental period." B's personal use of the unit is similarly taken into account in applying section 280A(c)(5) to any other use of the unit during the taxable year, e.g., the use of a portion of the unit as a place of business. >