

partner disposes of a partnership interest the basis of which has been so reduced, the partner's basis in such interest shall be increased, immediately before such disposition, by the amount that any such basis reductions exceed any amount of disallowed business interest that has been deducted by the partner against excess business interest income or excess taxable income of the same partnership.⁸⁸⁰

This special carryforward rule does not apply to S corporations and their shareholders.

Exceptions

The limitation does not apply to any taxpayer (other than a tax shelter prohibited from using the cash method under section 448(a)(3)) that meets the \$25 million gross receipts test of section 448(c) (*i.e.*, if the average annual gross receipts for the three-taxable-year period ending with the prior taxable year does not exceed \$25 million).⁸⁸¹ Aggregation rules apply to determine the amount of a taxpayer's gross receipts under the \$25 million gross receipts test.

The trade or business of performing services as an employee is not treated as a trade or business for purposes of the limitation.⁸⁸² As a result, for example, the wages of an employee are not counted in the adjusted taxable income of the taxpayer for purposes of determining the limitation.

At the taxpayer's election, any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business (*i.e.*, any electing real property trade or business) is not treated as a trade or business for purposes of the limitation, and therefore the limitation does not apply to such trades or businesses.⁸⁸³ Similarly, at the taxpayer's election, any farming business⁸⁸⁴ or

⁸⁸⁰ The special rule for dispositions also applies to transfers of a partnership interest (including by reason of death) in transactions in which gain is not recognized in whole or in part. No deduction is allowed to the transferor or transferee for any disallowed business interest resulting in a basis increase under this rule.

⁸⁸¹ In the case of a sole proprietorship, the \$25 million gross receipts test is applied as if the sole proprietorship were a corporation or partnership. For a discussion of changes made to section 448 by the Act, see the description of section 13102 of the Act (Small Business Accounting Method Reform and Simplification).

⁸⁸² The trade or business of performing services as an employee is also mentioned in section 62(a)(1), among other places, and has the same meaning here as there.

⁸⁸³ Congress intends that any such real property trade or business, including such a trade or business conducted by a corporation or REIT, be included. Because this description of a real property trade or business refers only to the section 469(c)(7)(C) description, and not to other rules of section 469 (such as the rule of section 469(c)(2) that passive activities include rental activities or the rule of section 469(a) that a passive activity loss is limited under section 469), the other rules of section 469 are not made applicable by this reference. It is further intended that a real property operation or a real property management trade or business includes the operation or management of a lodging facility, including a lodging facility that provides some supplemental services, such as an assisted living facility. In addition, an electing real property trade or business is required to use the alternative depreciation system ("ADS") to depreciate any of its nonresidential real property, residential rental property, qualified improvement property, qualified leasehold improvement property, qualified retail improvement property, and qualified restaurant property. See the description of section 13204 of the Act (Applicable Recovery Period for Real Property).

⁸⁸⁴ As defined in section 263A(e)(4) (*i.e.*, farming business means the trade or business of farming and includes the trade or business of operating a nursery or sod farm, or the raising or harvesting of trees bearing fruit, nuts, or other crops, or ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots)). Treas. Reg. sec. 1.263A-4(a)(4) further defines a farming business as a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity. Examples of a farming business include the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising