

(C) the alteration or termination of any instrument or agreement described in subparagraph (B), and

(D) gains from sales or exchanges of capital assets to the extent provided in subchapter P (sec. 1201 and following, relating to capital gains and losses).

(2) The gross income during the taxable year from any trade or business (other than an insurance business) carried on by the insurance company, or by a partnership of which the insurance company is a partner. In computing gross income under this paragraph, there shall be excluded any item described in paragraph (1).

(c) DEDUCTIONS.—In computing taxable investment income, the following deductions shall be allowed:

(1) TAX-FREE INTEREST.—The amount of interest which under section 103 is excluded for the taxable year from gross income.

(2) INVESTMENT EXPENSES.—Investment expenses paid or accrued during the taxable year. If any general expenses are in part assigned to or included in the investment expenses, the total deduction under this paragraph shall not exceed one-fourth of 1 percent of the mean of the book value of the invested assets held at the beginning and end of the taxable year plus one-fourth of the amount by which taxable investment income (computed without any deduction for investment expenses allowed by this paragraph, for tax-free interest allowed by paragraph (1), or for partially tax-exempt interest and dividends received allowed by paragraph (7)), exceeds 3¼ percent of the book value of the mean of the invested assets held at the beginning and end of the taxable year.

(3) REAL ESTATE EXPENSES.—Taxes (as provided in section 164), and other expenses, paid or accrued during the taxable year exclusively on or with respect to the real estate owned by the company. No deduction shall be allowed under this paragraph for any amount paid out for new buildings, or for permanent improvements or betterments made to increase the value of any property.

(4) DEPRECIATION.—The depreciation deduction allowed by section 167.

(5) INTEREST PAID OR ACCRUED.—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest on which is wholly exempt from taxation under this subtitle.