



P, a U.S. corporation, established a bonus program for the employees of its wholly owned domestic corporate subsidiary, S. Under the program, P pays cash bonuses in December of each year to S's employees for their past services performed for S during the calendar year. None of these employees perform any services for P.

P's payment to S's employees is treated as a contribution to S's capital accompanied by a constructive payment by S of the cash bonuses to its employees. Due to the deemed contribution and constructive payment, the cash bonuses may be deducted by S under section 162 of the Code, provided that each employee's total compensation is reasonable for the services performed.