''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section and section 1056 of Title 29, Labor] shall apply to plan years beginning on or after October 1, 2008.

''(2) SPECIAL RULE.—In the case of a plan for which the valuation date is not the first day of the plan year, the amendments made by this section shall apply to plan years beginning after December 31, 2007.''

EFFECTIVE DATE OF 2008 AMENDMENT

Amendment by Pub. L. 110–458 effective as if included in the provisions of Pub. L. 109–280 to which the amendment relates, except as otherwise provided, see section 112 of Pub. L. 110–458, set out as a note under section 72 of this title.

EFFECTIVE DATE

Pub. L. 109–280, title I, §113(b), Aug. 17, 2006, 120 Stat. 852, as amended by Pub. L. 110–458, title I, §101(c)(3), Dec. 23, 2008, 122 Stat. 5098, provided that:

''(1) IN GENERAL.—The amendments made by this section [enacting this subpart] shall apply to plan years beginning after December 31, 2007.

''(2) COLLECTIVE BARGAINING EXCEPTION.—In the case of a plan maintained pursuant to 1 or more collective bargaining agreements between employee representatives and 1 or more employers ratified before January 1, 2008, the amendments made by this section shall not apply to plan years beginning before the earlier of—

''(A) the later of—

''(i) the date on which the last collective bargaining agreement relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act [Aug. 17, 2006]), or

''(ii) the first day of the first plan year to which the amendments made by this section [enacting this subpart] would (but for this paragraph) apply, or

''(B) January 1, 2010.

For purposes of subparagraph (A)(i), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section shall not be treated as a termination of such collective bargaining agreement.''

PROVISIONS RELATING TO PLAN AMENDMENTS

Pub. L. 113–159, title II, §2003(c)(4), Aug. 8, 2014, 128 Stat. 1850, provided that:

''(A) IN GENERAL.—If this paragraph applies to any amendment to any plan or annuity contract, such plan or contract shall be treated as being operated in accordance with the terms of the plan during the period described in subparagraph (B)(ii).

''(B) AMENDMENTS TO WHICH PARAGRAPH APPLIES.—

''(i) IN GENERAL.—This paragraph shall apply to any amendment to any plan or annuity contract which is made—

''(I) pursuant to the amendments made by this subsection [amending this section and section 1056 of Title 29, Labor], or pursuant to any regulation issued by the Secretary of the Treasury or the Secretary of Labor under any provision as so amended, and

''(II) on or before the last day of the first plan year beginning on or after January 1, 2016, or such later date as the Secretary of the Treasury may prescribe.

''(ii) CONDITIONS.—This subsection [amending this section and section 1056 of Title 29, Labor, and enacting provisions set out as a note under this section] shall not apply to any amendment unless, during the period—

''(I) beginning on the date that the amendments made by this subsection or the regulation described in clause (i)(I) takes effect (or in the case of a plan or contract amendment not required by such amendments or such regulation, the effective date specified by the plan), and

''(II) ending on the date described in clause (i)(II) (or, if earlier, the date the plan or contract amendment is adopted),

the plan or contract is operated as if such plan or contract amendment were in effect, and such plan or contract amendment applies retroactively for such period.

''(C) ANTI-CUTBACK RELIEF.—A plan shall not be treated as failing to meet the requirements of section 204(g) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1054(g)) and section 411(d)(6) of the Internal Revenue Code of 1986 [26 U.S.C. 411(d)(6)] solely by reason of a plan amendment to which this paragraph applies.''

TEMPORARY MODIFICATION OF APPLICATION OF LIMITATION ON BENEFIT ACCRUALS

Pub. L. 111–192, title II, §203(b), June 25, 2010, 124 Stat. 1300, provided that: ''Section 203 of the Worker, Retiree, and Employer Recovery Act of 2008 [Pub. L. 110–458, set out below] shall apply to a plan for any plan year in lieu of the amendments made by this section applying to sections 206(g)(4) of the Employee Retirement Income Security Act of 1974 [29 U.S.C. 1056(g)(4)] and 436(e) of the Internal Revenue Code of 1986 only to the extent that such section produces a higher adjusted funding target attainment percentage for such plan for such year.''

Pub. L. 110–458, title II, §203, Dec. 23, 2008, 122 Stat. 5118, provided that: ''In the case of the first plan year beginning during the period beginning on October 1, 2008, and ending on September 30, 2009, sections 206(g)(4)(A) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1056(g)(4)(A)) and 436(e)(1) of the Internal Revenue Code of 1986 shall be applied by substituting the plan's adjusted funding target attainment percentage for the preceding plan year for such percentage for such plan year but only if the adjusted funding target attainment percentage for the preceding plan year is greater.''

APPLICABILITY OF AMENDMENTS BY SUBTITLES A AND B OF TITLE I OF PUB. L. 109–280

For special rules on applicability of amendments by subtitles A (§§101–108) and B (§§111–116) of title I of Pub. L. 109–280 to certain eligible cooperative plans, PBGC settlement plans, and eligible government contractor plans, see sections 104, 105, and 106 of Pub. L. 109–280, set out as notes under section 401 of this title.

Subchapter E—Accounting Periods and Methods of Accounting

PART I—ACCOUNTING PERIODS

AMENDMENTS

1987—Pub. L. 100–203, title X, §10206(a)(2), Dec. 22, 1987, 101 Stat. 1330–398, added item 444.

§ 441. Period for computation of taxable income

(a) Computation of taxable income

Taxable income shall be computed on the basis of the taxpayer's taxable year.

(b) Taxable year

For purposes of this subtitle, the term ''taxable year'' means—

(1) the taxpayer's annual accounting period, if it is a calendar year or a fiscal year;

(2) the calendar year, if subsection (g) applies;

(3) the period for which the return is made, if a return is made for a period of less than 12 months; or

(4) in the case of a DISC filing a return for a period of at least 12 months, the period determined under subsection (h).

(c) Annual accounting period

For purposes of this subtitle, the term ''annual accounting period'' means the annual period on the basis of which the taxpayer regularly computes his income in keeping his books.

(d) Calendar year

For purposes of this subtitle, the term ''calendar year'' means a period of 12 months ending on December 31.

(e) Fiscal year

For purposes of this subtitle, the term ''fiscal year'' means a period of 12 months ending on the last day of any month other than December. In the case of any taxpayer who has made the election provided by subsection (f) the term means the annual period (varying from 52 to 53 weeks) so elected.

(f) Election of year consisting of 52–53 weeks

(1) General rule

A taxpayer who, in keeping his books, regularly computes his income on the basis of an annual period which varies from 52 to 53 weeks and ends always on the same day of the week and ends always—

(A) on whatever date such same day of the week last occurs in a calendar month, or

(B) on whatever date such same day of the week falls which is nearest to the last day of a calendar month,

may (in accordance with the regulations prescribed under paragraph (3)) elect to compute his taxable income for purposes of this subtitle on the basis of such annual period. This paragraph shall apply to taxable years ending after the date of the enactment of this title.

(2) Special rules for 52–53-week year

(A) Effective dates

In any case in which the effective date or the applicability of any provision of this title is expressed in terms of taxable years beginning, including, or ending with reference to a specified date which is the first or last day of a month, a taxable year described in paragraph (1) shall (except for purposes of the computation under section 15) be treated—

(i) as beginning with the first day of the calendar month beginning nearest to the first day of such taxable year, or

(ii) as ending with the last day of the calendar month ending nearest to the last day of such taxable year,

as the case may be.

(B) Change in accounting period

In the case of a change from or to a taxable year described in paragraph (1)—

(i) if such change results in a short period (within the meaning of section 443) of 359 days or more, or of less than 7 days, section 443(b) (relating to alternative tax computation) shall not apply;

(ii) if such change results in a short period of less than 7 days, such short period shall, for purposes of this subtitle, be added to and deemed a part of the following taxable year; and

(iii) if such change results in a short period to which subsection (b) of section 443 applies, the taxable income for such short period shall be placed on an annual basis for purposes of such subsection by multiplying the gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions as described in section 443(c)) by 365, by dividing the result by the number of days in the short period, and the tax shall be the same part of the tax computed on the annual basis as the number of days in the short period is of 365 days.

(3) Special rule for partnerships, S corporations, and personal service corporations

The Secretary may by regulation provide terms and conditions for the application of this subsection to a partnership, S corporation, or personal service corporation (within the meaning of section 441(i)(2)).

(4) Regulations

The Secretary shall prescribe such regulations as he deems necessary for the application of this subsection.

(g) No books kept; no accounting period

Except as provided in section 443 (relating to returns for periods of less than 12 months), the taxpayer's taxable year shall be the calendar year if—

(1) the taxpayer keeps no books;

(2) the taxpayer does not have an annual accounting period; or

(3) the taxpayer has an annual accounting period, but such period does not qualify as a fiscal year.

(h) Taxable year of DISC's

(1) In general

For purposes of this subtitle, the taxable year of any DISC shall be the taxable year of that shareholder (or group of shareholders with the same 12-month taxable year) who has the highest percentage of voting power.

(2) Special rule where more than one shareholder (or group) has highest percentage

If 2 or more shareholders (or groups) have the highest percentage of voting power under paragraph (1), the taxable year of the DISC shall be the same 12-month period as that of any such shareholder (or group).

(3) Subsequent changes of ownership

The Secretary shall prescribe regulations under which paragraphs (1) and (2) shall apply to a change of ownership of a corporation after the taxable year of the corporation has been

determined under paragraph (1) or (2) only if such change is a substantial change of ownership.

(4) Voting power determined

For purposes of this subsection, voting power shall be determined on the basis of total combined voting power of all classes of stock of the corporation entitled to vote.

(i) Taxable year of personal service corporations

(1) In general

For purposes of this subtitle, the taxable year of any personal service corporation shall be the calendar year unless the corporation establishes, to the satisfaction of the Secretary, a business purpose for having a different period for its taxable year. For purposes of this paragraph, any deferral of income to shareholders shall not be treated as a business purpose.

(2) Personal service corporation

For purposes of this subsection, the term ''personal service corporation'' has the meaning given such term by section 269A(b)(1), except that section 269A(b)(2) shall be applied—

(A) by substituting ''any'' for ''more than 10 percent'', and

(B) by substituting ''any'' for ''50 percent or more in value'' in section 318(a)(2)(C).

A corporation shall not be treated as a personal service corporation unless more than 10 percent of the stock (by value) in such corporation is held by employee-owners (within the meaning of section 269A(b)(2), as modified by the preceding sentence). If a corporation is a member of an affiliated group filing a consolidated return, all members of such group shall be taken into account in determining whether such corporation is a personal service corporation.

(Aug. 16, 1954, ch. 736, 68A Stat. 148; Pub. L. 88–272, title II, §235(c)(3), Feb. 26, 1964, 78 Stat. 127; Pub. L. 94–455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 95–30, title I, §102(b)(5), May 23, 1977, 91 Stat. 137; Pub. L. 98–369, div. A, title IV, §474(b)(2), title VIII, §803, July 18, 1984, 98 Stat. 830, 1000; Pub. L. 99–514, title I, §104(b)(6), title VIII, §806(c)(1), (d), Oct. 22, 1986, 100 Stat. 2105, 2364; Pub. L. 100–647, title I, §1008(e)(4), Nov. 10, 1988, 102 Stat. 3440; Pub. L. 110–172, §11(g)(7), Dec. 29, 2007, 121 Stat. 2490.)

AMENDMENTS

2007—Subsec. (b)(4). Pub. L. 110–172, §11(g)(7)(A), struck out ''FSC or'' before ''DISC filing''.

Subsec. (h). Pub. L. 110–172, §11(g)(7)(B), struck out ''FSC's and'' before ''DISC's'' in heading and ''FSC or'' before ''DISC'' in pars. (1) and (2).

1988—Subsec. (i)(2). Pub. L. 100–647 inserted at end ''A corporation shall not be treated as a personal service corporation unless more than 10 percent of the stock (by value) in such corporation is held by employee-owners (within the meaning of section 269A(b)(2), as modified by the preceding sentence). If a corporation is a member of an affiliated group filing a consolidated return, all members of such group shall be taken into account in determining whether such corporation is a personal service corporation.''

1986—Subsec. (f)(2)(B)(iii). Pub. L. 99–514, §104(b)(6), struck out ''and by adding the zero bracket amount,'' after ''in the short period,''.

Subsec. (f)(3), (4). Pub. L. 99–514, §806(d), added par. (3) and redesignated former par. (3) as (4).

Subsec. (i). Pub. L. 99–514, §806(c)(1), added subsec. (i).

1984—Subsec. (b)(4). Pub. L. 98–369, §803(a), added par. (4).

Subsec. (f)(2)(A). Pub. L. 98–369, §474(b)(2), substituted ''section 15'' for ''section 21'' in provisions preceding cl. (i).

Subsec. (h). Pub. L. 98–369, §803(b), added subsec. (h).

1977—Subsec. (f)(2)(B)(iii). Pub. L. 95–30 substituted ''multiplying the gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions as described in section 443(c)) by 365, by dividing the result by the number of days in the short period, and by adding the zero bracket amount'' for ''multiplying such income by 365 and dividing the result by the number of days in the short period''.

1976—Subsec. (f)(3). Pub. L. 94–455 struck out ''or his delegate'' after ''Secretary''.

1964—Subsec. (f)(2)(A). Pub. L. 88–272 inserted '', including,'' before ''or ending with reference to''.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 104(b)(6) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, see section 151(a) of Pub. L. 99–514, set out as a note under section 1 of this title.

Amendment by section 806(c)(1), (d) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, with special provisions applicable to taxpayers who are required to change their accounting periods, see section 806(e) of Pub. L. 99–514, set out as a note under section 1378 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 474(b)(2) of Pub. L. 98–369 applicable to taxable years beginning after Dec. 31, 1983, and to carrybacks from such years, see section 475(a) of Pub. L. 98–369, set out as a note under section 21 of this title.

Amendment by section 803 of Pub. L. 98–369 applicable to taxable years beginning after Dec. 31, 1984, see section 805(a)(4) of Pub. L. 98–369, as amended, set out as a note under section 245 of this title.

EFFECTIVE DATE OF 1977 AMENDMENT

Amendment by Pub. L. 95–30 applicable to taxable years beginning after Dec. 31, 1976, see section 106(a) of Pub. L. 95–30, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1964 AMENDMENT

Amendment by Pub. L. 88–272 applicable to taxable years ending after Dec. 31, 1963, see section 235(d) of Pub. L. 88–272, set out as a note under section 269 of this title.

CONSTRUCTION OF SECTION 806 OF PUB. L. 99–514

Nothing in section 806 of Pub. L. 99–514 or in any legislative history relating thereto to be construed as requiring the Secretary of the Treasury or his delegate to permit an automatic change of a taxable year, see section 1008(e)(9) of Pub. L. 100–647, set out as a note under section 1378 of this title.

§ 442. Change of annual accounting period

If a taxpayer changes his annual accounting period, the new accounting period shall become

the taxpayer's taxable year only if the change is approved by the Secretary. For purposes of this subtitle, if a taxpayer to whom section 441(g) applies adopts an annual accounting period (as defined in section 441(c)) other than a calendar year, the taxpayer shall be treated as having changed his annual accounting period.

(Aug. 16, 1954, ch. 736, 68A Stat. 149; Pub. L. 94–455, title XIX, § 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834.)

AMENDMENTS

1976—Pub. L. 94–455 struck out ''or his delegate'' after ''Secretary''.

§ 443. Returns for a period of less than 12 months

(a) Returns for short period

A return for a period of less than 12 months (referred to in this section as ''short period'') shall be made under any of the following circumstances:

(1) Change of annual accounting period

When the taxpayer, with the approval of the Secretary, changes his annual accounting period. In such a case, the return shall be made for the short period beginning on the day after the close of the former taxable year and ending at the close of the day before the day designated as the first day of the new taxable year.

(2) Taxpayer not in existence for entire taxable year

When the taxpayer is in existence during only part of what would otherwise be his taxable year.

(b) Computation of tax on change of annual accounting period

(1) General rule

If a return is made under paragraph (1) of subsection (a), the taxable income for the short period shall be placed on an annual basis by multiplying the modified taxable income for such short period by 12, dividing the result by the number of months in the short period. The tax shall be the same part of the tax computed on the annual basis as the number of months in the short period is of 12 months.

(2) Exception

(A) Computation based on 12-month period

If the taxpayer applies for the benefits of this paragraph and establishes the amount of this taxable income for the 12-month period described in subparagraph (B), computed as if that period were a taxable year and under the law applicable to that year, then the tax for the short period, computed under paragraph (1), shall be reduced to the greater of the following:

(i) an amount which bears the same ratio to the tax computed on the taxable income for the 12-month period as the modified taxable income computed on the basis of the short period bears to the modified taxable income for the 12-month period; or

(ii) the tax computed on the modified taxable income for the short period.

The taxpayer (other than a taxpayer to whom subparagraph (B)(ii) applies) shall compute the tax and file his return without the application of this paragraph.

(B) 12-month period

The 12-month period referred to in subparagraph (A) shall be—

(i) the period of 12 months beginning on the first day of the short period, or

(ii) the period of 12 months ending at the close of the last day of the short period, if at the end of the 12 months referred to in clause (i) the taxpayer is not in existence or (if a corporation) has theretofore disposed of substantially all of its assets.

(C) Application for benefits

Application for the benefits of this paragraph shall be made in such manner and at such time as the regulations prescribed under subparagraph (D) may require; except that the time so prescribed shall not be later than the time (including extensions) for filing the return for the first taxable year which ends on or after the day which is 12 months after the first day of the short period. Such application, in case the return was filed without regard to this paragraph, shall be considered a claim for credit or refund with respect to the amount by which the tax is reduced under this paragraph.

(D) Regulations

The Secretary shall prescribe such regulations as he deems necessary for the application of this paragraph.

(3) Modified taxable income defined

For purposes of this subsection the term ''modified taxable income'' means, with respect to any period, the gross income for such period minus the deductions allowed by this chapter for such period (but, in the case of a short period, only the adjusted amount of the deductions for personal exemptions).

(c) Adjustment in deduction for personal exemption

In the case of a taxpayer other than a corporation, if a return is made for a short period by reason of subsection (a)(1) and if the tax is not computed under subsection (b)(2), then the exemptions allowed as a deduction under section 151 (and any deduction in lieu thereof) shall be reduced to amounts which bear the same ratio to the full exemptions as the number of months in the short period bears to 12.

(d) Adjustment in computing minimum tax and tax preferences

If a return is made for a short period by reason of subsection (a)—

(1) the alternative minimum taxable income for the short period shall be placed on an annual basis by multiplying such amount by 12 and dividing the result by the number of months in the short period, and

(2) the amount computed under paragraph (1) of section 55(a) shall bear the same relation to the tax computed on the annual basis as the number of months in the short period bears to 12.

(e) Cross references

For inapplicability of subsection (b) in computing—

(1) Accumulated earnings tax, see section 536.

(2) Personal holding company tax, see section 546.

(3) The taxable income of a regulated investment company, see section 852(b)(2)(E).

(4) The taxable income of a real estate investment trust, see section 857(b)(2)(C).

For returns for a period of less than 12 months in the case of a debtor's election to terminate a taxable year, see section 1398(d)(2)(E).

(Aug. 16, 1954, ch. 736, 68A Stat. 149; Pub. L. 86–779, §10(i), Sept. 14, 1960, 74 Stat. 1009; Pub. L. 91–172, title III, §301(b)(6), Dec. 30, 1969, 83 Stat. 585; Pub. L. 94–455, title III, §301(e), title XII, §1204(c)(2), title XVI, §1607(b)(1)(C), title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1553, 1697, 1757, 1834; Pub. L. 95–30, title I, §102(b)(6), May 23, 1977, 91 Stat. 137; Pub. L. 95–600, title IV, §421(e)(2), title VII, §703(*o*)(1)–(3), Nov. 6, 1978, 92 Stat. 2876, 2943; Pub. L. 96–222, title I, §104(a)(4)(H)(iii), Apr. 1, 1980, 94 Stat. 217; Pub. L. 96–589, §3(d), Dec. 24, 1980, 94 Stat. 3401; Pub. L. 97–448, title III, §304(a), Jan. 12, 1983, 96 Stat. 2398; Pub. L. 99–514, title I, §104(b)(7), title VII, §701(e)(3), Oct. 22, 1986, 100 Stat. 2105, 2342; Pub. L. 108–357, title IV, §413(c)(6), Oct. 22, 2004, 118 Stat. 1507.)

AMENDMENTS

2004—Subsec. (e)(3) to (5). Pub. L. 108–357 redesignated pars. (4) and (5) as (3) and (4), respectively, and struck out former par. (3) which read as follows: ''Undistributed foreign personal holding company income, see section 557.''

1986—Subsec. (b)(1). Pub. L. 99–514, §104(b)(7)(A), struck out '', and adding the zero bracket amount'' after ''by the number of months in the short period''.

Subsec. (b)(2)(A)(ii). Pub. L. 99–514, §104(b)(7)(B), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: ''the tax computed on the sum of the modified taxable income for the short period plus the zero bracket amount.''

Subsec. (d). Pub. L. 99–514, §701(e)(3), substituted ''and tax preferences'' for ''for tax preferences'' in heading and amended text generally. Prior to amendment, subsec. (d) read as follows: ''If a return is made for a short period by reason of subsection (a), then—

''(1) in the case of a taxpayer other than a corporation, the alternative minimum taxable income for the short period shall be placed on an annual basis by multiplying that amount by 12 and dividing the result by the number of months in the short period, and the amount computed under paragraph (1) of section 55(a) shall be the same part of the tax computed on the annual basis as the number of months in the short period is of 12 months; and

''(2) the $10,000 amount specified in section 56 (relating to minimum tax for tax preferences), modified as provided by section 58, shall be reduced to the amount which bears the same ratio to such specified amount as the number of days in the short period bears to 365.''

1983—Subsec. (e). Pub. L. 97–448 substituted ''section 1398(d)(2)(E)'' for ''section 1398(d)(3)(E)''.

1980—Subsec. (d)(2). Pub. L. 96–222 struck out ''in the case of a corporation,'' before ''the $10,000 amount''.

Subsec. (e). Pub. L. 96–589 inserted cross reference to section 1398(d)(3)(E) for returns for a period of less than 12 months in the case of a debtor's election to terminate a taxable year.

1978—Subsec. (b)(1). Pub. L. 95–600, §703(*o*)(2), substituted ''modified taxable income for such short period'' for ''gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions)''.

Subsec. (b)(2). Pub. L. 95–600, §703(*o*)(1), substituted in cl. (i) ''modified taxable income'' for ''taxable income'' in two places and in cl. (ii) ''the sum of the modified taxable income'' for ''the taxable income'' and ''plus the zero bracket amount'' for ''without placing the taxable income on an annual basis''.

Subsec. (b)(3). Pub. L. 95–600, §703(*o*)(3), added par. (3).

Subsec. (d). Pub. L. 95–600, §421(e)(2), substituted ''Adjustment in computing minimum tax for tax preferences'' for ''Adjustment in exclusion for computing minimum tax for tax preferences'' in heading, redesignated existing provisions as par. (2) and as so redesignated applied par. (2) to corporations, and added par. (1).

1977—Subsec. (b)(1). Pub. L. 95–30 substituted ''multiplying the gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions) by 12, dividing the result by the number of months in the short period, and adding the zero bracket amount'' for ''multiplying such income by 12, and dividing the result by the number of months in the short period''.

1976—Subsec. (a)(1). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary''.

Subsec. (a)(3). Pub. L. 94–455, §1204(c)(2), struck out par. (3) which made termination of taxpayer's taxable year under section 6851 as one of the circumstances under which a tax return for a period of less than 12 months shall be made.

Subsec. (b)(2)(D). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary''.

Subsec. (d). Pub. L. 94–455, §301(e), substituted ''$10,000'' for ''$30,000''.

Subsec. (e)(5). Pub. L. 94–455, §1607(b)(1)(C), substituted ''section 857(b)(2)(C)'' for ''section 857(b)(2)(D)''.

1969—Subsecs. (d), (e). Pub. L. 91–172 added subsec. (d) and redesignated former subsec. (d) as (e).

1960—Subsec. (d)(5). Pub. L. 86–779 added par. (5).

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108–357 applicable to taxable years of foreign corporations beginning after Dec. 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end, see section 413(d)(1) of Pub. L. 108–357, set out as an Effective and Termination Dates of 2004 Amendments note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 104(b)(7) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, see section 151(a) of Pub. L. 99–514, set out as a note under section 1 of this title.

Amendment by section 701(e)(3) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, with certain exceptions and qualifications, see section 701(f) of Pub. L. 99–514, set out as an Effective Date note under section 55 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Pub. L. 97–448, title III, §311(b)(1), Jan. 12, 1983, 96 Stat. 2411, provided that: ''The amendment made by subsection (a) of section 304 [amending this section] shall take effect as if included in the amendments made by section 3 of the Bankruptcy Tax Act of 1980 [section 3 of Pub. L. 96–589, which amended this section and sections 6012 and 6103 of this title].''

EFFECTIVE DATE OF 1980 AMENDMENT

Amendment by Pub. L. 96–589 applicable to bankruptcy cases commencing more than 90 days after Dec. 24, 1980, see section 7(b) of Pub. L. 96–589, set out as a note under section 108 of this title.

Amendment by Pub. L. 96–222 effective, except as otherwise provided, as if it had been included in the provisions of the Revenue Act of 1978, Pub. L. 95–600, to which such amendment relates, see section 201 of Pub. L. 96–222, set out as a note under section 32 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Pub. L. 95–600, title VII, §703(*o*)(4), Nov. 6, 1978, 92 Stat. 2943, provided that: ''The amendments made by

this subsection [amending this section] shall apply to taxable years beginning after December 31, 1976.''

Amendment by section 421(e)(2) of Pub. L. 95–600 applicable to taxable years beginning after Dec. 31, 1978, see section 421(g) of Pub. L. 95–600, set out as a note under section 5 of this title.

EFFECTIVE DATE OF 1977 AMENDMENT

Amendment by Pub. L. 95–30 applicable to taxable years beginning after Dec. 31, 1976, see section 106(a) of Pub. L. 95–30, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

Pub. L. 94–455, title III, § 301(g)(1), Oct. 4, 1976, 90 Stat. 1553, provided that the amendment made by section 301(e) of Pub. L. 94–455 is effective for items of tax preferences for taxable years beginning after Dec. 31, 1975, with certain exceptions.

Amendment by section 1204(c)(2) of Pub. L. 94–455 effective with respect to action taken under section 6851, 6861, or 6862 of this title where the notice and demand takes place after Feb. 28, 1977, see section 1204(d) of Pub. L. 94–455, as amended, set out as a note under section 6851 of this title.

For effective date of amendment by section 1607(b)(1)(C) of Pub. L. 94–455, see section 1608(c) of Pub. L. 94–455, set out as a note under section 857 of this title.

EFFECTIVE DATE OF 1969 AMENDMENT

Amendment by Pub. L. 91–172 applicable to taxable years ending after Dec. 31, 1969, see section 301(c) of Pub. L. 91–172, set out as a note under section 5 of this title.

EFFECTIVE DATE OF 1960 AMENDMENT

Amendment by Pub. L. 86–779 applicable with respect to taxable years of real estate investment trusts beginning after Dec. 31, 1960, see section 10(k) of Pub. L. 86–779, set out as an Effective Date note under section 856 of this title.

APPLICABILITY OF CERTAIN AMENDMENTS BY PUB. L. 99–514 IN RELATION TO TREATY OBLIGATIONS OF UNITED STATES

For applicability of amendment by section 701(e)(3) of Pub. L. 99–514 notwithstanding any treaty obligation of the United States in effect on Oct. 22, 1986, see section 1012(aa)(2) of Pub. L. 100–647, set out as a note under section 861 of this title.

§ 444. Election of taxable year other than required taxable year

(a) General rule

Except as otherwise provided in this section, a partnership, S corporation, or personal service corporation may elect to have a taxable year other than the required taxable year.

(b) Limitations on taxable years which may be elected

(1) In general

Except as provided in paragraphs (2) and (3), an election may be made under subsection (a) only if the deferral period of the taxable year elected is not longer than 3 months.

(2) Changes in taxable year

Except as provided in paragraph (3), in the case of an entity changing a taxable year, an election may be made under subsection (a) only if the deferral period of the taxable year elected is not longer than the shorter of—

(A) 3 months, or

(B) the deferral period of the taxable year which is being changed.

(3) Special rule for entities retaining 1986 taxable years

In the case of an entity's 1st taxable year beginning after December 31, 1986, an entity may elect a taxable year under subsection (a) which is the same as the entity's last taxable year beginning in 1986.

(4) Deferral period

For purposes of this subsection, except as provided in regulations, the term ''deferral period'' means, with respect to any taxable year of the entity, the months between—

(A) the beginning of such year, and

(B) the close of the 1st required taxable year ending within such year.

(c) Effect of election

If an entity makes an election under subsection (a), then—

(1) in the case of a partnership or S corporation, such entity shall make the payments required by section 7519, and

(2) in the case of a personal service corporation, such corporation shall be subject to the deduction limitations of section 280H.

(d) Elections

(1) Person making election

An election under subsection (a) shall be made by the partnership, S corporation, or personal service corporation.

(2) Period of election

(A) In general

Any election under subsection (a) shall remain in effect until the partnership, S corporation, or personal service corporation changes its taxable year or otherwise terminates such election. Any change to a required taxable year may be made without the consent of the Secretary.

(B) No further election

If an election is terminated under subparagraph (A) or paragraph (3)(A), the partnership, S corporation, or personal service corporation may not make another election under subsection (a).

(3) Tiered structures, etc.

(A) In general

Except as otherwise provided in this paragraph—

(i) no election may be under subsection (a) with respect to any entity which is part of a tiered structure, and

(ii) an election under subsection (a) with respect to any entity shall be terminated if such entity becomes part of a tiered structure.

(B) Exceptions for structures consisting of certain entities with same taxable year

Subparagraph (A) shall not apply to any tiered structure which consists only of partnerships or S corporations (or both) all of which have the same taxable year.

(e) Required taxable year

For purposes of this section, the term ''required taxable year'' means the taxable year de-

termined under section 706(b), 1378, or 441(i) without taking into account any taxable year which is allowable by reason of business purposes. Solely for purposes of the preceding sentence, sections 706(b), 1378, and 441(i) shall be treated as in effect for taxable years beginning before January 1, 1987.

(f) Personal service corporation

For purposes of this section, the term ''personal service corporation'' has the meaning given to such term by section 441(i)(2).

(g) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section, including regulations to prevent the avoidance of subsection (b)(2)(B) or (d)(2)(B) through the change in form of an entity.

(Added Pub. L. 100–203, title X, §10206(a)(1), Dec. 22, 1987, 101 Stat. 1330–397; amended Pub. L. 100–647, title II, §2004(e)(1), (2)(A), (12), (13), Nov. 10, 1988, 102 Stat. 3600, 3602.)

AMENDMENTS

1988—Subsec. (a). Pub. L. 100–647, §2004(e)(1)(A), substituted ''as otherwise provided in this section'' for ''as provided in subsections (b) and (c)''.

Subsec. (b)(4). Pub. L. 100–647, §2004(e)(13), inserted ''except as provided in regulations,'' before ''the term''.

Subsec. (d)(2)(A). Pub. L. 100–647, §2004(e)(12), inserted ''or otherwise terminates such election'' after ''its taxable year''.

Subsec. (d)(2)(B). Pub. L. 100–647, §2004(e)(1)(C), inserted ''or paragraph (3)(A)'' after ''under subparagraph (A)''.

Subsec. (d)(3). Pub. L. 100–647, §2004(e)(1)(B), amended par. (3) generally. Prior to amendment, par. (3) read as follows: ''No election may be made under subsection (a) with respect to an entity which is part of a tiered structure other than a tiered structure comprised of 1 or more partnerships or S corporations all of which have the same taxable year.''

Subsecs. (f), (g). Pub. L. 100–647, §2004(e)(2)(A), added subsec. (f) and redesignated former subsec. (f) as (g).

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provisions of the Revenue Act of 1987, Pub. L. 100–203, title X, to which such amendment relates, see section 2004(u) of Pub. L. 100–647, set out as a note under section 56 of this title.

EFFECTIVE DATE

Pub. L. 100–203, title X, §10206(d), Dec. 22, 1987, 101 Stat. 1330–403, as amended by Pub. L. 100–647, title II, §2004(e)(11), Nov. 10, 1988, 102 Stat. 3602, provided that:

''(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [enacting this section and sections 280H and 7519 of this title] shall apply to taxable years beginning after December 31, 1986.

''(2) REQUIRED PAYMENTS.—The amendments made by subsection (b) [enacting section 7519 of this title] shall apply to applicable election years beginning after December 31, 1986.

''(3) ELECTIONS.—Any election under section 444 of the Internal Revenue Code of 1986 (as added by subsection (a)) for an entity's 1st taxable year beginning after December 31, 1986, shall not be required to be made before the 90th day after the date of the enactment of this Act [Dec. 22, 1987].

''(4) SPECIAL RULE FOR EXISTING ENTITIES ELECTING S CORPORATION STATUS.—If a C corporation (within the meaning of section 1361(a)(2) of the Internal Revenue Code of 1986) with a taxable year other than the calendar year—

''(A) made an election after September 18, 1986, and before January 1, 1988, under section 1362 of such Code to be treated as an S corporation, and

''(B) elected to have the calendar year as the taxable year of the S corporation,

then section 444(b)(2)(B) of such Code shall be applied by taking into account the deferral period of the last taxable year of the C corporation rather than the deferral period of the taxable year being changed. The preceding sentence shall apply only in the case of an election under section 444 of such Code made for a taxable year beginning before 1989.''

PART II—METHODS OF ACCOUNTING

SUBPART A—METHODS OF ACCOUNTING IN GENERAL

AMENDMENTS

1986—Pub. L. 99–514, title VIII, §801(c), Oct. 22, 1986, 100 Stat. 2348, added item 448.

1976—Pub. L. 94–455, title II, §207(c)(1)(B), Oct. 4, 1976, 90 Stat. 1541, added item 447.

§ 446. General rule for methods of accounting

(a) General rule

Taxable income shall be computed under the method of accounting on the basis of which the taxpayer regularly computes his income in keeping his books.

(b) Exceptions

If no method of accounting has been regularly used by the taxpayer, or if the method used does not clearly reflect income, the computation of taxable income shall be made under such method as, in the opinion of the Secretary, does clearly reflect income.

(c) Permissible methods

Subject to the provisions of subsections (a) and (b), a taxpayer may compute taxable income under any of the following methods of accounting—

(1) the cash receipts and disbursements method;

(2) an accrual method;

(3) any other method permitted by this chapter; or

(4) any combination of the foregoing methods permitted under regulations prescribed by the Secretary.

(d) Taxpayer engaged in more than one business

A taxpayer engaged in more than one trade or business may, in computing taxable income, use a different method of accounting for each trade or business.

(e) Requirement respecting change of accounting method

Except as otherwise expressly provided in this chapter, a taxpayer who changes the method of

accounting on the basis of which he regularly computes his income in keeping his books shall, before computing his taxable income under the new method, secure the consent of the Secretary.

(f) Failure to request change of method of accounting

If the taxpayer does not file with the Secretary a request to change the method of accounting, the absence of the consent of the Secretary to a change in the method of accounting shall not be taken into account—

(1) to prevent the imposition of any penalty, or the addition of any amount to tax, under this title, or

(2) to diminish the amount of such penalty or addition to tax.

(Aug. 16, 1954, ch. 736, 68A Stat. 151; Pub. L. 94–455, title XIX, § 1906 (b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 98–369, div. A, title I, § 161(a), July 18, 1984, 98 Stat. 696.)

AMENDMENTS

1984—Subsec. (f). Pub. L. 98–369 added subsec. (f).

1976—Subsecs. (b), (c), (e). Pub. L. 94–455 struck out ''or his delegate'' after ''Secretary''.

EFFECTIVE DATE OF 1984 AMENDMENT

Pub. L. 98–369, div. A, title I, § 161(b), July 18, 1984, 98 Stat. 697, provided that: ''The amendment made by this section [amending this section] shall apply to taxable years beginning after the date of the enactment of this Act [July 18, 1984].''

§ 447. Method of accounting for corporations engaged in farming

(a) General rule

Except as otherwise provided by law, the taxable income from farming of—

(1) a corporation engaged in the trade or business of farming, or

(2) a partnership engaged in the trade or business of farming, if a corporation is a partner in such partnership,

shall be computed on an accrual method of accounting. This section shall not apply to the trade or business of operating a nursery or sod farm or to the raising or harvesting of trees (other than fruit and nut trees).

(b) Preproductive period expenses

For rules requiring capitalization of certain preproductive period expenses, see section 263A.

(c) Exception for certain corporations

For purposes of subsection (a), a corporation shall be treated as not being a corporation for any taxable year if it is—

(1) an S corporation, or

(2) a corporation which meets the gross receipts test of section 448(c) for such taxable year.

(d) Coordination with section 481

Any change in method of accounting made pursuant to this section shall be treated for purposes of section 481 as initiated by the taxpayer and made with the consent of the Secretary.

(e) Certain annual accrual accounting methods

(1) In general

Notwithstanding subsection (a) or section 263A, if—

(A) for its 10 taxable years ending with its first taxable year beginning after December 31, 1975, a corporation or qualified partnership used an annual accrual method of accounting with respect to its trade or business of farming,

(B) such corporation or qualified partnership raises crops which are harvested not less than 12 months after planting, and

(C) such corporation or qualified partnership has used such method of accounting for all taxable years intervening between its first taxable year beginning after December 31, 1975, and the taxable year,

such corporation or qualified partnership may continue to employ such method of accounting for the taxable year with respect to its qualified farming trade or business.

(2) Annual accrual method of accounting defined

For purposes of paragraph (1), the term ''annual accrual method of accounting'' means a method under which revenues, costs, and expenses are computed on an accrual method of accounting and the preproductive period expenses incurred during the taxable year are charged to harvested crops or deducted in determining the taxable income for such years.

(3) Certain nonrecognition transfers

For purposes of this subsection, if—

(A) a corporation acquired substantially all the assets of a qualified farming trade or business from another corporation in a transaction in which no gain or loss was recognized to the transferor or transferee corporation, or

(B) a qualified partnership acquired substantially all the assets of a qualified farming trade or business from one of its partners in a transaction to which section 721 applies,

the transferee corporation or qualified partnership shall be deemed to have computed its taxable income on an annual accrual method of accounting during the period for which the transferor corporation or partnership computed its taxable income from such trade or business on an annual accrual method.

(4) Qualified partnership defined

For purposes of this subsection—

(A) Qualified partnership

The term ''qualified partnership'' means a partnership which is engaged in a qualified farming trade or business and each of the partners of which is a corporation other than—

(i) an S corporation, or

(ii) a personal holding company (within the meaning of section 542(a)).

(B) Qualified farming trade or business

(i) In general

The term ''qualified farming trade or business'' means the trade or business of farming—

(I) sugar cane,

(II) any plant with a preproductive period (as defined in section 263A(e)(3)) of 2 years or less, and

(III) any other plant (other than any citrus or almond tree) if an election by the corporation under this subparagraph is in effect.

In the case of a partnership and for purposes of paragraph (3)(A), subclauses (II) and (III) shall not apply.

(ii) Effect of election

For purposes of paragraphs (1) and (2) of section 263A(e), any election under this subparagraph shall be treated as if it were an election under subsection (d)(3) of section 263A.

(iii) Election

Unless the Secretary otherwise consents, an election under this subparagraph may be made only for the corporation's 1st taxable year which begins after December 31, 1986, and during which the corporation engages in a farming business. Any such election, once made, may be revoked only with the consent of the Secretary.

(Added Pub. L. 94–455, title II, §207(c)(1)(A), Oct. 4, 1976, 90 Stat. 1538; amended Pub. L. 95–600, title III, §§351(a), 353(a), title VII, §§701(*l*)(1), 703(d), Nov. 6, 1978, 92 Stat. 2846, 2847, 2906, 2939; Pub. L. 97–248, title II, §230(a), Sept. 3, 1982, 96 Stat. 495; Pub. L. 97–354, §5(a)(28), (29), Oct. 19, 1982, 96 Stat. 1695; Pub. L. 99–514, title VIII, §803(b)(7), Oct. 22, 1986, 100 Stat. 2356; Pub. L. 100–203, title X, §10205(a)–(c), Dec. 22, 1987, 101 Stat. 1330–395 to 1330–397; Pub. L. 100–647, title I, §1008(b)(5), (6), Nov. 10, 1988, 102 Stat. 3438; Pub. L. 101–508, title XI, §11702(b), Nov. 5, 1990, 104 Stat. 1388–514; Pub. L. 105–34, title X, §1081(a), Aug. 5, 1997, 111 Stat. 949; Pub. L. 115–97, title I, §13102(a)(5), Dec. 22, 2017, 131 Stat. 2102.)

AMENDMENTS

2017—Subsec. (c). Pub. L. 115–97, §13102(a)(5)(A)(i), in introductory provisions, inserted ''for any taxable year'' after ''not being a corporation''.

Subsec. (c)(2). Pub. L. 115–97, §13102(a)(5)(A)(ii), amended par. (2) generally. Prior to amendment, par. (2) read as follows: ''a corporation the gross receipts of which meet the requirements of subsection (d).''

Subsec. (d). Pub. L. 115–97, §13102(a)(5)(C), redesignated subsec. (f) as (d) and struck out former subsec. (d) which related to gross receipts requirements.

Subsec. (e). Pub. L. 115–97, §13102(a)(5)(C), redesignated subsec. (g) as (e) and struck out former subsec. (e) which related to members of the same family.

Subsec. (f). Pub. L. 115–97, §13102(a)(5)(C)(ii), redesignated subsec. (f) as (d).

Pub. L. 115–97, §13102(a)(5)(B), amended subsec. (f) generally. Prior to amendment, subsec. (f) related to coordination with section 481.

Subsec. (g). Pub. L. 115–97, §13102(a)(5)(C)(ii), redesignated subsec. (g) as (e).

Subsecs. (h), (i). Pub. L. 115–97, §13102(a)(5)(C)(i), struck out subsecs. (h) and (i) which related to exception for certain closely held corporations and suspense account for family corporations, respectively.

1997—Subsec. (i)(3). Pub. L. 105–34 redesignated par. (5) as (3) and struck out heading and text of former par. (3). Text read as follows: ''If—

''(A) the gross receipts of the corporation from the trade or business of farming for the year of the change or any subsequent taxable year, is less than

''(B) such gross receipts for the taxpayer's last taxable year beginning before the year of the change (or for the most recent taxable year for which a reduction in the suspense account was made under this paragraph),

the amount in the suspense account (after taking into account prior reductions) shall be reduced by the percentage by which the amount described in subparagraph (A) is less than the amount described in subparagraph (B).''

Subsec. (i)(4). Pub. L. 105–34 redesignated par. (6) as (4) and struck out heading and text of former par. (4). Text read as follows: ''Any reduction in the suspense account under paragraph (3) shall be included in gross income for the taxable year of the reduction.''

Subsec. (i)(5), (6). Pub. L. 105–34 added par. (5) and redesignated former pars. (5) and (6) as (3) and (4), respectively.

1990—Subsec. (g)(1)(A). Pub. L. 101–508, §11702(b)(2), substituted ''trade or business of farming'' for ''qualified farming trade or business''.

Subsec. (g)(4)(B). Pub. L. 101–508, §11702(b)(1), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: ''The term 'qualified farming trade or business' means the trade or business of farming sugar cane.''

1988—Subsec. (b). Pub. L. 100–647, §1008(b)(5), substituted ''period expenses'' for ''period of expenses'' in heading and in text.

Subsec. (g)(1). Pub. L. 100–647, §1008(b)(6), substituted ''qualified farming trade or business'' for ''trade or business of farming'' in subpar. (A) and in concluding provisions.

1987—Subsec. (c). Pub. L. 100–203, §10205(a), added subsec. (c), substituting ''certain corporations'' for ''small business and family corporations'' in heading and striking out former text which read as follows: ''For purposes of subsection (a), a corporation shall be treated as not being a corporation if it is—

''(1) an S corporation,

''(2) a corporation of which at least 50 percent of the total combined voting power of all classes of stock entitled to vote, and at least 50 percent of the total number of shares of all other classes of stock of the corporation, are owned by members of the same family, or

''(3) a corporation the gross receipts of which meet the requirements of subsection (e).''

Subsec. (d). Pub. L. 100–203, §10205(a), added subsec. (d). Former subsec. (d) redesignated (e).

Subsec. (e). Pub. L. 100–203, §10205(c)(1), substituted ''subsection (d)'' for ''subsection (c)(2)''.

Pub. L. 100–203, §10205(a), redesignated former subsec. (d) as (e) and struck out former subsec. (e), ''Corporation having gross receipts of $1,000,000 or less'', which read as follows: ''A corporation meets the requirements of this subsection if, for each prior taxable year beginning after December 31, 1975, such corporation (and any predecessor corporation) did not have gross receipts exceeding $1,000,000. For purposes of the preceding sentence, all corporations which are members of a controlled group of corporations (within the meaning of section 1563(a)) shall be treated as one corporation.''

Subsec. (h)(1). Pub. L. 100–203, §10205(c)(2)(A), substituted ''A corporation is described in this subsection'' for ''This section shall not apply to any corporation''.

Subsec. (h)(1)(A), (B). Pub. L. 100–203, §10205(c)(2)(B), (C), substituted ''subsection (e)'' for ''subsection (d)'' and ''subsection (e)(1)'' for ''subsection (d)(1)'' wherever appearing.

Subsec. (i). Pub. L. 100–203, §10205(b), added subsec. (i).

1986—Subsec. (a). Pub. L. 99–514, §803(b)(7)(B), which directed that subsec. (a) be amended by striking out ''and with the capitalization of preproductive period of expenses described in subsection (b)'', was executed by striking out ''and with the capitalization of preproductive period expenses described in subsection (b)'' after ''accrual method of accounting'', as the probable intent of Congress.

Subsec. (b). Pub. L. 99–514, §803(b)(7)(A), in amending subsec. (b) generally, substituted in heading ''period of expenses'' for ''period expenses'' and in text the cross

reference to section 263A for former par. (1) defining ''preproductive period expenses'', par. (2) relating to exceptions, and par. (3) defining ''preproductive period''.

Subsec. (g)(1). Pub. L. 99–514, § 803(b)(7)(C), substituted ''Notwithstanding subsection (a) or section 263A, if'' for ''If''.

1982—Subsec. (c)(1). Pub. L. 97–354, § 5(a)(28), substituted ''an S corporation'' for ''an electing small business corporation (within the meaning of section 1371(b))''.

Subsec. (g)(1). Pub. L. 97–248, § 230(a)(1), inserted ''or qualified partnership'' after ''corporation'' wherever appearing.

Subsec. (g)(3). Pub. L. 97–248, § 230(a)(2), designated existing provisions from ''a corporation acquired'' through ''transferee corporation'', as subpar. (A), inserted ''qualified'' before ''farming trade'', and added subpar. (B).

Subsec. (g)(4). Pub. L. 97–354, § 5(a)(29), substituted in subpar. (A)(i) ''an S corporation'' for ''an electing small business corporation (within the meaning of section 1371(b))''.

Pub. L. 97–248, § 230(a)(3), added par. (4).

1978—Subsec. (a). Pub. L. 95–600, §§ 353(a), 703(d), substituted in provisions following par. (2) ''preproductive period expenses'' for ''preproductive expenses'' and ''nursery or sod farm'' for ''nursery''.

Subsec. (f)(3). Pub. L. 95–600, § 701(*l*)(1), struck out ''(except as otherwise provided in such regulations)'' before ''be taken'' and inserted ''(or the remaining taxable years where there is a stated future life of less than 10 taxable years)'' after ''10 taxable years''.

Subsec. (g)(2). Pub. L. 95–600, § 703(d), substituted ''preproductive period expenses'' for ''preproductive expenses''.

Subsec. (h). Pub. L. 95–600, § 351(a), added subsec. (h).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, with provision for preservation of suspense account rules with respect to any existing suspense accounts, see section 13102(e) of Pub. L. 115–97, set out as a note under section 263A of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105–34, title X, § 1081(b), Aug. 5, 1997, 111 Stat. 950, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years ending after June 8, 1997.''

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101–508 effective as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 11702(j) of Pub. L. 101–508, set out as a note under section 59 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1987 AMENDMENT

Pub. L. 100–203, title X, § 10205(d), Dec. 22, 1987, 101 Stat. 1330–397, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1987.''

EFFECTIVE DATE OF 1986 AMENDMENT

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the amendment by Pub. L. 99–514 is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99–514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101–239, set out as an Effective Date note under section 263A of this title.

Amendment by Pub. L. 99–514 applicable to costs incurred after Dec. 31, 1986, in taxable years ending after such date, except as otherwise provided, see section 803(d) of Pub. L. 99–514, set out as an Effective Date note under section 263A of this title.

EFFECTIVE DATE OF 1982 AMENDMENT

Amendment by Pub. L. 97–354 applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97–354, set out as an Effective Date note under section 1361 of this title.

Pub. L. 97–248, title II, § 230(b), Sept. 3, 1982, 96 Stat. 496, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1981.''

EFFECTIVE DATE OF 1978 AMENDMENT

Pub. L. 95–600, title III, § 351(b), Nov. 6, 1978, 92 Stat. 2846, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1977.''

Pub. L. 95–600, title III, § 353(b), Nov. 6, 1978, 92 Stat. 2847, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1976.''

Pub. L. 95–600, title VII, § 703(*l*)(4), Nov. 6, 1978, 92 Stat. 2907, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that: ''The amendment made by paragraphs (1) [amending this section] and (3) [amending section 464 of this title] shall take effect as if included in section 447 or 464 (as the case may be) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] at the time of the enactment of such sections [Oct. 4, 1976].''

Amendment by section 703(d) of Pub. L. 95–600 effective on Oct. 4, 1976, see section 703(r) of Pub. L. 95–600, set out as a note under section 46 of this title.

EFFECTIVE DATE

Pub. L. 94–455, title II, § 207(c)(2), Oct. 4, 1976, 90 Stat. 1541, as amended by Pub. L. 95–30, title IV, § 404, May 23, 1977, 91 Stat. 155; Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by paragraph (1) [enacting this section] shall apply to taxable years beginning after December 31, 1976.

''(B) SPECIAL RULE FOR CERTAIN CORPORATIONS.—In the case of a corporation engaged in the trade or business of farming and with respect to which—

''(i) members of two families (within the meaning of paragraph (1) of [former] section 447(d) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954], as added by paragraph (1)) owned, on October 4, 1976 (directly or through the application of such [former] section 447(d)), at least 65 percent of the total combined voting power of all classes of stock of such corporation entitled to vote, and at least 65 percent of the total number of shares of all other classes of stock of such corporation; or

''(ii) members of three families (within the meaning of paragraph (1) of such [former] section 447(d)) owned, on October 4, 1976 (directly or through the application of such [former] section 447(d)), at least 50 percent of the total combined voting power of all classes of stock of such corporation entitled to vote, and at least 50 percent of the total number of shares of all other classes of stock of such corporation; and substantially all of the stock of such corporation which was not so owned (directly or through the application of such [former] section 447(d)), by members of such three families was owned, on October 4, 1976, directly—

''(I) by employees of the corporation or members of the families (within the meaning of section 267(c)(4) of such Code) of such employees, or

''(II) by a trust for the benefit of the employees of such corporation which is described in section 401(a) of such Code and which is exempt from taxation under section 501(a) of such Code,

the amendments made by paragraph (1) shall apply to taxable years beginning after December 31, 1977.''

ACCOUNTING FOR GROWING CROPS

Pub. L. 95–600, title III, § 352, Nov. 6, 1978, 92 Stat. 2846, provided that:

''(a) APPLICATION OF SECTION.—This section shall apply to a taxpayer who—

''(1) is a farmer, nurseryman, or florist,

''(2) is on an accrual method of accounting, and

''(3) is not required by section 447 of the Internal Revenue Code of 1954 to capitalize preproductive period expenses.

''(b) TAXPAYER MAY NOT BE REQUIRED TO INVENTORY GROWING CROPS.—A taxpayer to whom this section applies may not be required to inventory growing crops for any taxable year beginning after December 31, 1977.

''(c) TAXPAYER MAY ELECT TO CHANGE TO CASH METHOD.—A taxpayer to whom this section applies may, for any taxable year beginning after December 31, 1977 and before January 1, 1981, change to the cash receipts and disbursements method of accounting with respect to any trade or business in which the principal activity is growing crops.

''(d) SECTION 481 OF CODE TO APPLY.—Any change in the way in which a taxpayer accounts for the costs of growing crops resulting from the application of subsection (b) or (c)—

''(1) shall not require the consent of the Secretary of the Treasury or his delegate, and

''(2) shall be treated, for purposes of section 481 of the Internal Revenue Code of 1954 as a change in the method of accounting initiated by the taxpayer.

''(e) GROWING CROPS.—For purposes of this section, the term 'Growing crops' does not include trees grown for lumber, pulp, or other nonlife purposes.''

AUTOMATIC TEN-YEAR ADJUSTMENT FOR FARMING SYNDICATES CHANGING TO ACCRUAL ACCOUNTING

Pub. L. 95–600, title VII, § 703(*l*)(2), Nov. 6, 1978, 92 Stat. 2906, provided that: ''If—

''(A) a farming syndicate (within the meaning of [former] section 464(c) of the Internal Revenue Code of 1954 [now 26 U.S.C. 461(k)]) was in existence on December 31, 1975, and

''(B) such syndicate elects an accrual method of accounting (including the capitalization of preproductive period expenses described in section 447(b) of such Code) for a taxable year beginning before January 1, 1979,

then such election shall be treated as having been made with the consent of the Secretary of the Treasury or his delegate and, under regulations prescribed by the Secretary of the Treasury or his delegate, the net amount of the adjustments required by section 481(a) of such Code to be taken into account by the taxpayer in computing taxable income shall be taken into account in each of the 10 taxable years (or the remaining taxable years where there is a stated future life of less than 10 taxable years) beginning with the year of change.''

ELECTION TO CHANGE FROM STATIC VALUE METHOD TO ACCRUAL METHOD OF ACCOUNTING

Pub. L. 94–455, title II, § 207(c)(3), Oct. 4, 1976, 90 Stat. 1541, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(A) IN GENERAL.—If—

''(i) a corporation has computed its taxable income on an annual accrual method of accounting together with a static value method of accounting for deferred costs of growing crops for the 10 taxable years ending with its first taxable year beginning after December 31, 1975,

''(ii) such corporation raises crops which are harvested not less than 12 months after planting, and

''(iii) such corporation elects, within one year after the date of the enactment of this Act [Oct. 4, 1976] and in such manner as the Secretary of the Treasury or his delegate prescribes, to change to the annual accrual method of accounting (within the meaning of section 447(g)(2) [now section 447(e)(2)] of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]) for taxable years beginning after December 31, 1976,

such change shall be treated as having been made with the consent of the Secretary of the Treasury, and, under regulations prescribed by the Secretary of the Treasury or his delegate, the net amount of the adjustments required by section 481(a) of the Internal Revenue Code of 1986 to be taken into account by the taxpayer in computing taxable income shall (except as otherwise provided in such regulations) be taken into account in each of the 10 taxable years beginning with the year of change.

''(B) COORDINATION WITH SECTION 447 OF THE CODE.—A corporation which elects under subparagraph (A) to change to the annual accrual method of accounting shall, for purposes of section 447(g) [now section 447(e)] of the Internal Revenue Code of 1986, be deemed to be a corporation which has computed its taxable income on an annual accrual method of accounting for its 10 taxable years ending with its first taxable year beginning after December 31, 1975.

''(C) CERTAIN CORPORATE REORGANIZATIONS.—For purposes of this paragraph, if a corporation acquired substantially all the assets of a farming trade or business from another corporation in a transaction in which no gain or loss was recognized to the transferor or transferee corporation, the transferee corporation shall be deemed to have computed its taxable income on an annual accrual method of accounting together with a static value method of accounting for deferred costs of growing crops during the period for which the transferor corporation computed its taxable income from such trade or business on such accrual and static value method.''

§ 448. Limitation on use of cash method of accounting

(a) General rule

Except as otherwise provided in this section, in the case of a—

(1) C corporation,

(2) partnership which has a C corporation as a partner, or

(3) tax shelter,

taxable income shall not be computed under the cash receipts and disbursements method of accounting.

(b) Exceptions

(1) Farming business

Paragraphs (1) and (2) of subsection (a) shall not apply to any farming business.

(2) Qualified personal service corporations

Paragraphs (1) and (2) of subsection (a) shall not apply to a qualified personal service corporation, and such a corporation shall be treated as an individual for purposes of determining whether paragraph (2) of subsection (a) applies to any partnership.

(3) Entities which meet gross receipts test

Paragraphs (1) and (2) of subsection (a) shall not apply to any corporation or partnership for any taxable year if such entity (or any

predecessor) meets the gross receipts test of subsection (c) for such taxable year.

(c) Gross receipts test

For purposes of this section—

(1) In general

A corporation or partnership meets the gross receipts test of this subsection for any taxable year if the average annual gross receipts of such entity for the 3-taxable-year period ending with the taxable year which precedes such taxable year does not exceed $25,000,000.

(2) Aggregation rules

All persons treated as a single employer under subsection (a) or (b) of section 52 or subsection (m) or (*o*) of section 414 shall be treated as one person for purposes of paragraph (1).

(3) Special rules

For purposes of this subsection—

(A) Not in existence for entire 3-year period

If the entity was not in existence for the entire 3-year period referred to in paragraph (1), such paragraph shall be applied on the basis of the period during which such entity (or trade or business) was in existence.

(B) Short taxable years

Gross receipts for any taxable year of less than 12 months shall be annualized by multiplying the gross receipts for the short period by 12 and dividing the result by the number of months in the short period.

(C) Gross receipts

Gross receipts for any taxable year shall be reduced by returns and allowances made during such year.

(D) Treatment of predecessors

Any reference in this subsection to an entity shall include a reference to any predecessor of such entity.

(4) Adjustment for inflation

In the case of any taxable year beginning after December 31, 2018, the dollar amount in paragraph (1) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting ''calendar year 2017'' for ''calendar year 2016'' in subparagraph (A)(ii) thereof.

If any amount as increased under the preceding sentence is not a multiple of $1,000,000, such amount shall be rounded to the nearest multiple of $1,000,000.

(d) Definitions and special rules

For purposes of this section—

(1) Farming business

(A) In general

The term ''farming business'' means the trade or business of farming (within the meaning of section 263A(e)(4)).

(B) Timber and ornamental trees

The term ''farming business'' includes the raising, harvesting, or growing of trees to which section 263A(c)(5) applies.

(2) Qualified personal service corporation

The term ''qualified personal service corporation'' means any corporation—

(A) substantially all of the activities of which involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting, and

(B) substantially all of the stock of which (by value) is held directly (or indirectly through 1 or more partnerships, S corporations, or qualified personal service corporations not described in paragraph (2) or (3) of subsection (a)) by—

(i) employees performing services for such corporation in connection with the activities involving a field referred to in subparagraph (A),

(ii) retired employees who had performed such services for such corporation,

(iii) the estate of any individual described in clause (i) or (ii), or

(iv) any other person who acquired such stock by reason of the death of an individual described in clause (i) or (ii) (but only for the 2-year period beginning on the date of the death of such individual).

To the extent provided in regulations which shall be prescribed by the Secretary, indirect holdings through a trust shall be taken into account under subparagraph (B).

(3) Tax shelter defined

The term ''tax shelter'' has the meaning given such term by section 461(i)(3) (determined after application of paragraph (4) thereof). An S corporation shall not be treated as a tax shelter for purposes of this section merely by reason of being required to file a notice of exemption from registration with a State agency described in section 461(i)(3)(A), but only if there is a requirement applicable to all corporations offering securities for sale in the State that to be exempt from such registration the corporation must file such a notice.

(4) Special rules for application of paragraph (2)

For purposes of paragraph (2)—

(A) community property laws shall be disregarded,

(B) stock held by a plan described in section 401(a) which is exempt from tax under section 501(a) shall be treated as held by an employee described in paragraph (2)(B)(i), and

(C) at the election of the common parent of an affiliated group (within the meaning of section 1504(a)), all members of such group may be treated as 1 taxpayer for purposes of paragraph (2)(B) if 90 percent or more of the activities of such group involve the performance of services in the same field described in paragraph (2)(A).

(5) Special rule for certain services

(A) In general

In the case of any person using an accrual method of accounting with respect to amounts to be received for the performance of services by such person, such person shall

not be required to accrue any portion of such amounts which (on the basis of such person's experience) will not be collected if—

(i) such services are in fields referred to in paragraph (2)(A), or

(ii) such person meets the gross receipts test of subsection (c) for all prior taxable years.

(B) Exception

This paragraph shall not apply to any amount if interest is required to be paid on such amount or there is any penalty for failure to timely pay such amount.

(C) Regulations

The Secretary shall prescribe regulations to permit taxpayers to determine amounts referred to in subparagraph (A) using computations or formulas which, based on experience, accurately reflect the amount of income that will not be collected by such person. A taxpayer may adopt, or request consent of the Secretary to change to, a computation or formula that clearly reflects the taxpayer's experience. A request under the preceding sentence shall be approved if such computation or formula clearly reflects the taxpayer's experience.

(6) Treatment of certain trusts subject to tax on unrelated business income

For purposes of this section, a trust subject to tax under section 511(b) shall be treated as a C corporation with respect to its activities constituting an unrelated trade or business.

(7) Coordination with section 481

Any change in method of accounting made pursuant to this section shall be treated for purposes of section 481 as initiated by the taxpayer and made with the consent of the Secretary.

(8) Use of related parties, etc.

The Secretary shall prescribe such regulations as may be necessary to prevent the use of related parties, pass-thru entities, or intermediaries to avoid the application of this section.

(Added Pub. L. 99–514, title VIII, §801(a), Oct. 22, 1986, 100 Stat. 2345; amended Pub. L. 100–647, title I, §1008(a)(1), (2), (7)–(9), title VI, §6032(a), Nov. 10, 1988, 102 Stat. 3436, 3437, 3695; Pub. L. 107–147, title IV, §403(a), Mar. 9, 2002, 116 Stat. 40; Pub. L. 115–97, title I, §13102(a)(1)–(4), Dec. 22, 2017, 131 Stat. 2102.)

INFLATION ADJUSTED ITEMS FOR CERTAIN YEARS

For inflation adjustment of certain items in this section, see Revenue Procedures listed in a table under section 1 of this title.

AMENDMENTS

2017—Subsec. (b)(3). Pub. L. 115–97, §13102(a)(2), amended par. (3) generally. Prior to amendment, text read as follows: ''Paragraphs (1) and (2) of subsection (a) shall not apply to any corporation or partnership for any taxable year if, for all prior taxable years beginning after December 31, 1985, such entity (or any predecessor) met the $5,000,000 gross receipts test of subsection (c).''

Subsec. (c). Pub. L. 115–97, §13102(a)(1), substituted ''Gross receipts test'' for ''$5,000,000 gross receipts test'' in heading and amended introductory provisions and par. (1) generally. Prior to amendment, text read as follows: ''For purposes of this section—

''(1) IN GENERAL.—A corporation or partnership meets the $5,000,000 gross receipts test of this subsection for any prior taxable year if the average annual gross receipts of such entity for the 3-taxable-year period ending with such prior taxable year does not exceed $5,000,000.''

Subsec. (c)(4). Pub. L. 115–97, §13102(a)(3), added par. (4).

Subsec. (d)(7). Pub. L. 115–97, §13102(a)(4), amended par. (7) generally. Prior to amendment, par. (7) related to coordination with section 481.

2002—Subsec. (d)(5). Pub. L. 107–147 amended heading and text of par. (5) generally. Prior to amendment, text read as follows: ''In the case of any person using an accrual method of accounting with respect to amounts to be received for the performance of services by such person, such person shall not be required to accrue any portion of such amounts which (on the basis of experience) will not be collected. This paragraph shall not apply to any amount if interest is required to be paid on such amount or there is any penalty for failure to timely pay such amount.''

1988—Subsec. (c)(3)(D). Pub. L. 100–647, §1008(a)(9), added subpar. (D).

Subsec. (d)(2). Pub. L. 100–647, §6032(a), inserted at end ''To the extent provided in regulations which shall be prescribed by the Secretary, indirect holdings through a trust shall be taken into account under subparagraph (B).''

Subsec. (d)(2)(B). Pub. L. 100–647, §1008(a)(1)(A), substituted ''(or indirectly through 1 or more partnerships, S corporations, or qualified personal service corporations not described in paragraph (2) or (3) of subsection (a))'' for ''or indirectly''.

Subsec. (d)(3). Pub. L. 100–647, §1008(a)(7), inserted sentence at end relating to treatment of S corporation as tax shelter.

Subsec. (d)(4)(C). Pub. L. 100–647, §1008(a)(8), substituted ''90 percent or more of'' for ''substantially all of''.

Pub. L. 100–647, §1008(a)(2), substituted ''such group'' for ''all such members''.

Subsec. (d)(8). Pub. L. 100–647, §1008(a)(1)(B), added par. (8).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, see section 13102(e) of Pub. L. 115–97, set out as a note under section 263A of this title.

EFFECTIVE DATE OF 2002 AMENDMENT

Pub. L. 107–147, title IV, §403(b), Mar. 9, 2002, 116 Stat. 41, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to taxable years ending after the date of the enactment of this Act [Mar. 9, 2002].

''(2) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer required by the amendments made by this section to change its method of accounting for its first taxable year ending after the date of the enactment of this Act—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as made with the consent of the Secretary of the Treasury, and

''(C) the net amount of the adjustments required to be taken into account by the taxpayer under section 481 of the Internal Revenue Code of 1986 shall be taken into account over a period of 4 years (or if less, the number of taxable years that the taxpayer used the method permitted under section 448(d)(5) of such Code as in effect before the date of the enactment of this Act) beginning with such first taxable year.''

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1008(a)(1), (2), (7)–(9) of Pub. L. 100–647 effective, except as otherwise provided, as if in-

cluded in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Pub. L. 100–647, title VI, § 6032(b), Nov. 10, 1988, 102 Stat. 3695, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1986.''

EFFECTIVE DATE

Pub. L. 99–514, title VIII, § 801(d), Oct. 22, 1986, 100 Stat. 2348, as amended by Pub. L. 100–647, title I, § 1008(a)(5), (6), Nov. 10, 1988, 102 Stat. 3437, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [enacting this section and amending section 461 of this title] shall apply to taxable years beginning after December 31, 1986.

''(2) ELECTION TO RETAIN CASH METHOD FOR CERTAIN TRANSACTIONS.—A taxpayer may elect not to have the amendments made by this section apply to any loan or lease, or any transaction with a related party (within the meaning of section 267(b) of the Internal Revenue Code of 1954, as in effect before the enactment of this Act), entered into on or before September 25, 1985. Any election under the preceding sentence may be made separately with respect to each transaction.

''(3) CERTAIN CONTRACTS.—The amendments made by this section shall not apply to—

''(A) contracts for the acquisition or transfer of real property, and

''(B) contracts for services related to the acquisition or development of real property,

but only if such contracts were entered into before September 25, 1985, and the sole element of the contract which has not been performed as of September 25, 1985, is payment for such property or services.

''(4) TREATMENT OF AFFILIATED GROUP PROVIDING ENGINEERING SERVICES.—Each member of an affiliated group of corporations (within the meaning of section 1504(a) of the Internal Revenue Code of 1986) shall be allowed to use the cash receipts and disbursements method of accounting for any trade or business of providing engineering services with respect to taxable years ending after December 31, 1986, if the common parent of such group—

''(A) was incorporated in the State of Delaware in 1970,

''(B) was the successor to a corporation that was incorporated in the State of Illinois in 1949, and

''(C) used a method of accounting for long-term contracts of accounting [sic] for a substantial part of its income from the performance of engineering services.

''(5) SPECIAL RULE FOR PARAGRAPHS (2) AND (3).—If any loan, lease, contract, or evidence of any transaction to which paragraph (2) or (3) applies is transferred after June 10, 1987, to a person other than a related party (within the meaning of paragraph (2)), paragraph (2) or (3) shall cease to apply on and after the date of such transfer.''

SUBPART B—TAXABLE YEAR FOR WHICH ITEMS OF GROSS INCOME INCLUDED

AMENDMENTS

Pub. L. 110–343, div. C, title VIII, § 801(c), Oct. 3, 2008, 122 Stat. 3931, added item 457A.

1988—Pub. L. 100–647, title V, § 5076(b)(2), Nov. 10, 1988, 102 Stat. 3683, struck out ''of real property'' after ''rules for nondealers'' in item 453A.

1987—Pub. L. 100–203, title X, § 10202(a)(2), (c)(2), Dec. 22, 1987, 101 Stat. 1330–388, 1330–392, substituted ''Special rules for nondealers of real property'' for ''Installment method for dealers in personal property'' in item 453A, and struck out item 453C ''Certain indebtedness treated as payments on installment obligations''.

1986—Pub. L. 99–514, title XI, § 1107(b), (c), Oct. 22, 1986, 101 Stat. 2430, added item 457, applicable to taxable years beginning after Dec. 31, 1988, with certain exceptions, and struck out former item 457 ''Deferred compensation plans with respect to service for State and local governments''.

Pub. L. 99–514, title VIII, §§ 804(c), 811(b), Oct. 22, 1986, 100 Stat. 2361, 2368, added items 453C and 460.

1980—Pub. L. 96–471, § 2(d), Oct. 19, 1980, 94 Stat. 2254, added items 453 to 453B and struck out former item 453 ''Installment method''.

1978—Pub. L. 95–600, title I, § 131(b), title III, § 372(b), Nov. 6, 1978, 92 Stat. 2782, 2862, added items 457 and 458.

1961—Pub. L. 87–109, § 1(b), July 26, 1961, 75 Stat. 224, added item 456.

1958—Pub. L. 85–866, title I, § 28(b), Sept. 2, 1958, 72 Stat. 1626, added item 455, effective with respect to taxable years beginning after Dec. 31, 1957. See section 28(c) of Pub. L. 85–866 set out as an Effective Date note under section 455 of this title.

1955—Act June 15, 1955, ch. 143, § 2(2), 69 Stat. 135, struck out item 452 ''Adjustment in case of position inconsistent with prior income tax liability''.

§ 451. General rule for taxable year of inclusion

(a) General rule

The amount of any item of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under the method of accounting used in computing taxable income, such amount is to be properly accounted for as of a different period.

(b) Inclusion not later than for financial accounting purposes

(1) Income taken into account in financial statement

(A) In general

In the case of a taxpayer the taxable income of which is computed under an accrual method of accounting, the all events test with respect to any item of gross income (or portion thereof) shall not be treated as met any later than when such item (or portion thereof) is taken into account as revenue in—

(i) an applicable financial statement of the taxpayer, or

(ii) such other financial statement as the Secretary may specify for purposes of this subsection.

(B) Exception

This paragraph shall not apply to—

(i) a taxpayer which does not have a financial statement described in clause (i)

or (ii) of subparagraph (A) for a taxable year, or

(ii) any item of gross income in connection with a mortgage servicing contract.

(C) All events test

For purposes of this section, the all events test is met with respect to any item of gross income if all the events have occurred which fix the right to receive such income and the amount of such income can be determined with reasonable accuracy.

(2) Coordination with special methods of accounting

Paragraph (1) shall not apply with respect to any item of gross income for which the taxpayer uses a special method of accounting provided under any other provision of this chapter, other than any provision of part V of subchapter P (except as provided in clause (ii) of paragraph (1)(B)).

(3) Applicable financial statement

For purposes of this subsection, the term ''applicable financial statement'' means—

(A) a financial statement which is certified as being prepared in accordance with generally accepted accounting principles and which is—

(i) a 10–K (or successor form), or annual statement to shareholders, required to be filed by the taxpayer with the United States Securities and Exchange Commission,

(ii) an audited financial statement of the taxpayer which is used for—

(I) credit purposes,

(II) reporting to shareholders, partners, or other proprietors, or to beneficiaries, or

(III) any other substantial nontax purpose,

but only if there is no statement of the taxpayer described in clause (i), or

(iii) filed by the taxpayer with any other Federal agency for purposes other than Federal tax purposes, but only if there is no statement of the taxpayer described in clause (i) or (ii),

(B) a financial statement which is made on the basis of international financial reporting standards and is filed by the taxpayer with an agency of a foreign government which is equivalent to the United States Securities and Exchange Commission and which has reporting standards not less stringent than the standards required by such Commission, but only if there is no statement of the taxpayer described in subparagraph (A), or

(C) a financial statement filed by the taxpayer with any other regulatory or governmental body specified by the Secretary, but only if there is no statement of the taxpayer described in subparagraph (A) or (B).

(4) Allocation of transaction price

For purposes of this subsection, in the case of a contract which contains multiple performance obligations, the allocation of the transaction price to each performance obligation shall be equal to the amount allocated to each performance obligation for purposes of including such item in revenue in the applicable financial statement of the taxpayer.

(5) Group of entities

For purposes of paragraph (1), if the financial results of a taxpayer are reported on the applicable financial statement (as defined in paragraph (3)) for a group of entities, such statement shall be treated as the applicable financial statement of the taxpayer.

(c) Treatment of advance payments

(1) In general

A taxpayer which computes taxable income under the accrual method of accounting, and receives any advance payment during the taxable year, shall—

(A) except as provided in subparagraph (B), include such advance payment in gross income for such taxable year, or

(B) if the taxpayer elects the application of this subparagraph with respect to the category of advance payments to which such advance payment belongs, the taxpayer shall—

(i) to the extent that any portion of such advance payment is required under subsection (b) to be included in gross income in the taxable year in which such payment is received, so include such portion, and

(ii) include the remaining portion of such advance payment in gross income in the taxable year following the taxable year in which such payment is received.

(2) Election

(A) In general

Except as otherwise provided in this paragraph, the election under paragraph (1)(B) shall be made at such time, in such form and manner, and with respect to such categories of advance payments, as the Secretary may provide.

(B) Period to which election applies

An election under paragraph (1)(B) shall be effective for the taxable year with respect to which it is first made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to revoke such election. For purposes of this title, the computation of taxable income under an election made under paragraph (1)(B) shall be treated as a method of accounting.

(3) Taxpayers ceasing to exist

Except as otherwise provided by the Secretary, the election under paragraph (1)(B) shall not apply with respect to advance payments received by the taxpayer during a taxable year if such taxpayer ceases to exist during (or with the close of) such taxable year.

(4) Advance payment

For purposes of this subsection—

(A) In general

The term ''advance payment'' means any payment—

(i) the full inclusion of which in the gross income of the taxpayer for the tax-

able year of receipt is a permissible method of accounting under this section (determined without regard to this subsection),

(ii) any portion of which is included in revenue by the taxpayer in a financial statement described in clause (i) or (ii) of subsection (b)(1)(A) for a subsequent taxable year, and

(iii) which is for goods, services, or such other items as may be identified by the Secretary for purposes of this clause.

(B) Exclusions

Except as otherwise provided by the Secretary, such term shall not include—

(i) rent,

(ii) insurance premiums governed by subchapter L,

(iii) payments with respect to financial instruments,

(iv) payments with respect to warranty or guarantee contracts under which a third party is the primary obligor,

(v) payments subject to section 871(a), 881, 1441, or 1442,

(vi) payments in property to which section 83 applies, and

(vii) any other payment identified by the Secretary for purposes of this subparagraph.

(C) Receipt

For purposes of this subsection, an item of gross income is received by the taxpayer if it is actually or constructively received, or if it is due and payable to the taxpayer.

(D) Allocation of transaction price

For purposes of this subsection, rules similar to subsection (b)(4) shall apply.

(d) Special rule in case of death

In the case of the death of a taxpayer whose taxable income is computed under an accrual method of accounting, any amount accrued only by reason of the death of the taxpayer shall not be included in computing taxable income for the period in which falls the date of the taxpayer's death.

(e) Special rule for employee tips

For purposes of subsection (a), tips included in a written statement furnished an employer by an employee pursuant to section 6053(a) shall be deemed to be received at the time the written statement including such tips is furnished to the employer.

(f) Special rule for crop insurance proceeds or disaster payments

In the case of insurance proceeds received as a result of destruction or damage to crops, a taxpayer reporting on the cash receipts and disbursements method of accounting may elect to include such proceeds in income for the taxable year following the taxable year of destruction or damage, if he establishes that, under his practice, income from such crops would have been reported in a following taxable year. For purposes of the preceding sentence, payments received under the Agricultural Act of 1949, as amended, or title II of the Disaster Assistance Act of 1988, as a result of (1) destruction or damage to crops caused by drought, flood, or any other natural disaster, or (2) the inability to plant crops because of such a natural disaster shall be treated as insurance proceeds received as a result of destruction or damage to crops. An election under this subsection for any taxable year shall be made at such time and in such manner as the Secretary prescribes.

(g) Special rule for proceeds from livestock sold on account of drought, flood, or other weather-related conditions

(1) In general

In the case of income derived from the sale or exchange of livestock in excess of the number the taxpayer would sell if he followed his usual business practices, a taxpayer reporting on the cash receipts and disbursements method of accounting may elect to include such income for the taxable year following the taxable year in which such sale or exchange occurs if he establishes that, under his usual business practices, the sale or exchange would not have occurred in the taxable year in which it occurred if it were not for drought, flood, or other weather-related conditions, and that such conditions had resulted in the area being designated as eligible for assistance by the Federal Government.

(2) Limitation

Paragraph (1) shall apply only to a taxpayer whose principal trade or business is farming (within the meaning of section 6420(c)(3)).

(3) Special election rules

If section 1033(e)(2) applies to a sale or exchange of livestock described in paragraph (1), the election under paragraph (1) shall be deemed valid if made during the replacement period described in such section.

(h) Special rule for utility services

(1) In general

In the case of a taxpayer the taxable income of which is computed under an accrual method of accounting, any income attributable to the sale or furnishing of utility services to customers shall be included in gross income not later than the taxable year in which such services are provided to such customers.

(2) Definition and special rule

For purposes of this subsection—

(A) Utility services

The term ''utility services'' includes—

(i) the providing of electrical energy, water, or sewage disposal,

(ii) the furnishing of gas or steam through a local distribution system,

(iii) telephone or other communication services, and

(iv) the transporting of gas or steam by pipeline.

(B) Year in which services provided

The taxable year in which services are treated as provided to customers shall not, in any manner, be determined by reference to—

(i) the period in which the customers' meters are read, or

(ii) the period in which the taxpayer bills (or may bill) the customers for such service.

(i) Treatment of interest on frozen deposits in certain financial institutions

(1) In general

In the case of interest credited during any calendar year on a frozen deposit in a qualified financial institution, the amount of such interest includible in the gross income of a qualified individual shall not exceed the sum of—

(A) the net amount withdrawn by such individual from such deposit during such calendar year, and

(B) the amount of such deposit which is withdrawable as of the close of the taxable year (determined without regard to any penalty for premature withdrawals of a time deposit).

(2) Interest tested each year

Any interest not included in gross income by reason of paragraph (1) shall be treated as credited in the next calendar year.

(3) Deferral of interest deduction

No deduction shall be allowed to any qualified financial institution for interest not includible in gross income under paragraph (1) until such interest is includible in gross income.

(4) Frozen deposit

For purposes of this subsection, the term ''frozen deposit'' means any deposit if, as of the close of the calendar year, any portion of such deposit may not be withdrawn because of—

(A) the bankruptcy or insolvency of the qualified financial institution (or threat thereof), or

(B) any requirement imposed by the State in which such institution is located by reason of the bankruptcy or insolvency (or threat thereof) of 1 or more financial institutions in the State.

(5) Other definitions

For purposes of this subsection, the terms ''qualified individual'', ''qualified financial institution'', and ''deposit'' have the same respective meanings as when used in section 165(*l*).

(j) Special rule for cash options for receipt of qualified prizes

(1) In general

For purposes of this title, in the case of an individual on the cash receipts and disbursements method of accounting, a qualified prize option shall be disregarded in determining the taxable year for which any portion of the qualified prize is properly includible in gross income of the taxpayer.

(2) Qualified prize option; qualified prize

For purposes of this subsection—

(A) In general

The term ''qualified prize option'' means an option which—

(i) entitles an individual to receive a single cash payment in lieu of receiving a qualified prize (or remaining portion thereof), and

(ii) is exercisable not later than 60 days after such individual becomes entitled to the qualified prize.

(B) Qualified prize

The term ''qualified prize'' means any prize or award which—

(i) is awarded as a part of a contest, lottery, jackpot, game, or other similar arrangement,

(ii) does not relate to any past services performed by the recipient and does not require the recipient to perform any substantial future service, and

(iii) is payable over a period of at least 10 years.

(3) Partnership, etc.

The Secretary shall provide for the application of this subsection in the case of a partnership or other pass-through entity consisting entirely of individuals described in paragraph (1).

(k) Special rule for sales or dispositions to implement Federal Energy Regulatory Commission or State electric restructuring policy

(1) In general

In the case of any qualifying electric transmission transaction for which the taxpayer elects the application of this section, qualified gain from such transaction shall be recognized—

(A) in the taxable year which includes the date of such transaction to the extent the amount realized from such transaction exceeds—

(i) the cost of exempt utility property which is purchased by the taxpayer during the 4-year period beginning on such date, reduced (but not below zero) by

(ii) any portion of such cost previously taken into account under this subsection, and

(B) ratably over the 8-taxable year period beginning with the taxable year which includes the date of such transaction, in the case of any such gain not recognized under subparagraph (A).

(2) Qualified gain

For purposes of this subsection, the term ''qualified gain'' means, with respect to any qualifying electric transmission transaction in any taxable year—

(A) any ordinary income derived from such transaction which would be required to be recognized under section 1245 or 1250 for such taxable year (determined without regard to this subsection), and

(B) any income derived from such transaction in excess of the amount described in subparagraph (A) which is required to be included in gross income for such taxable year (determined without regard to this subsection).

(3) Qualifying electric transmission transaction

For purposes of this subsection, the term ''qualifying electric transmission transaction''

means any sale or other disposition before January 1, 2008 (before January 1, 2021, in the case of a qualified electric utility), of—

(A) property used in the trade or business of providing electric transmission services, or

(B) any stock or partnership interest in a corporation or partnership, as the case may be, whose principal trade or business consists of providing electric transmission services,

but only if such sale or disposition is to an independent transmission company.

(4) Independent transmission company

For purposes of this subsection, the term ''independent transmission company'' means—

(A) an independent transmission provider approved by the Federal Energy Regulatory Commission,

(B) a person—

(i) who the Federal Energy Regulatory Commission determines in its authorization of the transaction under section 203 of the Federal Power Act (16 U.S.C. 824b) or by declaratory order is not a market participant within the meaning of such Commission's rules applicable to independent transmission providers, and

(ii) whose transmission facilities to which the election under this subsection applies are under the operational control of a Federal Energy Regulatory Commission-approved independent transmission provider before the close of the period specified in such authorization, but not later than the date which is 4 years after the close of the taxable year in which the transaction occurs, or

(C) in the case of facilities subject to the jurisdiction of the Public Utility Commission of Texas—

(i) a person which is approved by that Commission as consistent with Texas State law regarding an independent transmission provider, or

(ii) a political subdivision or affiliate thereof whose transmission facilities are under the operational control of a person described in clause (i).

(5) Exempt utility property

For purposes of this subsection:

(A) In general

The term ''exempt utility property'' means property used in the trade or business of—

(i) generating, transmitting, distributing, or selling electricity, or

(ii) producing, transmitting, distributing, or selling natural gas.

(B) Nonrecognition of gain by reason of acquisition of stock

Acquisition of control of a corporation shall be taken into account under this subsection with respect to a qualifying electric transmission transaction only if the principal trade or business of such corporation is a trade or business referred to in subparagraph (A).

(C) Exception for property located outside the United States

The term ''exempt utility property'' shall not include any property which is located outside the United States.

(6) Qualified electric utility

For purposes of this subsection, the term ''qualified electric utility'' means a person that, as of the date of the qualifying electric transmission transaction, is vertically integrated, in that it is both—

(A) a transmitting utility (as defined in section 3(23) of the Federal Power Act (16 U.S.C. 796(23))) with respect to the transmission facilities to which the election under this subsection applies, and

(B) an electric utility (as defined in section 3(22) of the Federal Power Act (16 U.S.C. 796(22))).

(7) Special rule for consolidated groups

In the case of a corporation which is a member of an affiliated group filing a consolidated return, any exempt utility property purchased by another member of such group shall be treated as purchased by such corporation for purposes of applying paragraph (1)(A).

(8) Time for assessment of deficiencies

If the taxpayer has made the election under paragraph (1) and any gain is recognized by such taxpayer as provided in paragraph (1)(B), then—

(A) the statutory period for the assessment of any deficiency, for any taxable year in which any part of the gain on the transaction is realized, attributable to such gain shall not expire prior to the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may by regulations prescribe) of the purchase of exempt utility property or of an intention not to purchase such property, and

(B) such deficiency may be assessed before the expiration of such 3-year period notwithstanding any law or rule of law which would otherwise prevent such assessment.

(9) Purchase

For purposes of this subsection, the taxpayer shall be considered to have purchased any property if the unadjusted basis of such property is its cost within the meaning of section 1012.

(10) Election

An election under paragraph (1) shall be made at such time and in such manner as the Secretary may require and, once made, shall be irrevocable.

(11) Nonapplication of installment sales treatment

Section 453 shall not apply to any qualifying electric transmission transaction with respect to which an election to apply this subsection is made.

(Aug. 16, 1954, ch. 736, 68A Stat. 152; Pub. L. 89–97, title III, § 313(b), July 30, 1965, 79 Stat. 382; Pub. L. 91–172, title II, § 215(a), Dec. 30, 1969, 83 Stat. 573; Pub. L. 94–455, title XIX, § 1906(b)(13)(A),

title XXI, §§2102(a), (b), 2141(a), Oct. 4, 1976, 90 Stat. 1834, 1900, 1933; Pub. L. 99–514, title VIII, §821(a), title IX, §905(b), Oct. 22, 1986, 100 Stat. 2372, 2386; Pub. L. 100–647, title I, §1009(d)(3), title VI, §§6030(a), 6033(a), Nov. 10, 1988, 102 Stat. 3450, 3694, 3695; Pub. L. 105–34, title IX, §913(a), Aug. 5, 1997, 111 Stat. 878; Pub. L. 105–277, div. J, title V, §5301(a), Oct. 21, 1998, 112 Stat. 2681–918; Pub. L. 108–357, title III, §311(c), title VIII, §909(a), Oct. 22, 2004, 118 Stat. 1467, 1657; Pub. L. 109–58, title XIII, §1305(a), (b), Aug. 8, 2005, 119 Stat. 997; Pub. L. 110–343, div. B, title I, §109(a)–(c), Oct. 3, 2008, 122 Stat. 3821; Pub. L. 111–312, title VII, §705(a), Dec. 17, 2010, 124 Stat. 3311; Pub. L. 112–240, title IV, §411(a), Jan. 2, 2013, 126 Stat. 2343; Pub. L. 113–295, div. A, title I, §159(a), Dec. 19, 2014, 128 Stat. 4022; Pub. L. 114–113, div. Q, title I, §191(a), Dec. 18, 2015, 129 Stat. 3075; Pub. L. 115–97, title I, §13221(a), (b), Dec. 22, 2017, 131 Stat. 2113, 2115; Pub. L. 115–123, div. D, title I, §40414(a), Feb. 9, 2018, 132 Stat. 152; Pub. L. 116–94, div. Q, title I, §132(a), Dec. 20, 2019, 133 Stat. 3233.)

REFERENCES IN TEXT

The Agricultural Act of 1949, as amended, referred to in subsec. (f), is act Oct. 31, 1949, ch. 792, 63 Stat. 1051, as amended, which is classified principally to chapter 35A (§1421 et seq.) of Title 7, Agriculture. For complete classification of this Act to the Code, see Short Title note set out under section 1421 of Title 7 and Tables.

The Disaster Assistance Act of 1988, referred to in subsec. (f), is Pub. L. 100–387, Aug. 11, 1988, 102 Stat. 924. Title II of the Disaster Assistance Act of 1988 is set out as a note under section 1421 of Title 7. For complete classification of this Act to the Code, see Tables.

AMENDMENTS

2019—Subsec. (k)(3). Pub. L. 116–94 substituted ''January 1, 2021'' for ''January 1, 2018'' in introductory provisions.

2018—Subsec. (k)(3). Pub. L. 115–123 substituted ''January 1, 2018'' for ''January 1, 2017'' in introductory provisions.

2017—Subsecs. (b) to (k). Pub. L. 115–97 first added subsec. (b) and then added subsec. (c) and correspondingly redesignated former subsecs. (b) to (i) first as (c) to (j) and then as (d) to (k), respectively.

2015—Subsec. (i)(3). Pub. L. 114–113 substituted ''January 1, 2017'' for ''January 1, 2015'' in introductory provisions.

2014—Subsec. (i)(3). Pub. L. 113–295 substituted ''January 1, 2015'' for ''January 1, 2014'' in introductory provisions.

2013—Subsec. (i)(3). Pub. L. 112–240 substituted ''January 1, 2014'' for ''January 1, 2012'' in introductory provisions.

2010—Subsec. (i)(3). Pub. L. 111–312 substituted ''January 1, 2012'' for ''January 1, 2010'' in introductory provisions.

2008—Subsec. (i)(3). Pub. L. 110–343, §109(a)(1), inserted ''(before January 1, 2010, in the case of a qualified electric utility)'' after ''January 1, 2008'' in introductory provisions.

Subsec. (i)(4)(B)(ii). Pub. L. 110–343, §109(b), substituted ''the date which is 4 years after the close of the taxable year in which the transaction occurs'' for ''December 31, 2007''.

Subsec. (i)(5)(C). Pub. L. 110–343, §109(c), added subpar. (C).

Subsec. (i)(6) to (11). Pub. L. 110–343, §109(a)(2), added par. (6) and redesignated former pars. (6) to (10) as (7) to (11), respectively.

2005—Subsec. (i)(3). Pub. L. 109–58, §1305(a), substituted ''2008'' for ''2007'' in introductory provisions.

Subsec. (i)(4)(B)(ii). Pub. L. 109–58, §1305(b), substituted ''December 31, 2007'' for ''the close of the period applicable under subsection (a)(2)(B) as extended under paragraph (2)''.

2004—Subsec. (e)(3). Pub. L. 108–357, §311(c), added par. (3).

Subsec. (i). Pub. L. 108–357, §909(a), added subsec. (i).

1998—Subsec. (h). Pub. L. 105–277 added subsec. (h).

1997—Subsec. (e). Pub. L. 105–34 inserted '', flood, or other weather-related conditions'' after ''drought'' in heading and substituted ''drought, flood, or other weather-related conditions, and that such conditions'' for ''drought conditions, and that these drought conditions'' in par. (1).

1988—Subsec. (d). Pub. L. 100–647, §6033(a), inserted ''or title II of the Disaster Assistance Act of 1988,'' after ''the Agricultural Act of 1949, as amended,''.

Subsec. (e)(1). Pub. L. 100–647, §6030(a), struck out ''(other than livestock described in section 1231(b)(3))'' after ''exchange of livestock''.

Subsecs. (f), (g). Pub. L. 100–647, §1009(d)(3), redesignated subsec. (f), relating to treatment of interest on frozen deposits in certain financial institutions, as (g).

1986—Subsec. (f). Pub. L. 99–514, §905(b), added subsec. (f) relating to treatment of interest on frozen deposits in certain financial institutions.

Pub. L. 99–514, §821(a), added subsec. (f) relating to special rule for utility services.

1976—Subsec. (d). Pub. L. 94–455, §§1906(b)(13)(A), 2102(a), (b), inserted reference to disaster payments in heading, provided that payments received under the Agricultural Act of 1949, as amended, be treated as insurance proceeds received as a result of destruction or damage to crops if the payments are received as the result of destruction or damage from drought, flood, or other natural disaster, or as the result of inability to plant crops because of drought, flood, or other natural disaster, and struck out ''or his delegate'' after ''Secretary''.

Subsec. (e). Pub. L. 94–455, §2141(a), added subsec. (e).

1969—Subsec. (d). Pub. L. 91–172 added subsec. (d).

1965—Subsec. (c). Pub. L. 89–97 added subsec. (c).

EFFECTIVE DATE OF 2019 AMENDMENT

Pub. L. 116–94, div. Q, title I, §132(b), Dec. 20, 2019, 133 Stat. 3233, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2017.''

EFFECTIVE DATE OF 2018 AMENDMENT

Pub. L. 115–123, div. D, title I, §40414(b), Feb. 9, 2018, 132 Stat. 152, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2016.''

EFFECTIVE DATE OF 2017 AMENDMENT

Pub. L. 115–97, title I, §13221(c)–(e), Dec. 22, 2017, 131 Stat. 2116, 2117, provided that:

''(c) EFFECTIVE DATE.—The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2017.

''(d) COORDINATION WITH SECTION 481.—

''(1) IN GENERAL.—In the case of any qualified change in method of accounting for the taxpayer's first taxable year beginning after December 31, 2017—

''(A) such change shall be treated as initiated by the taxpayer, and

''(B) such change shall be treated as made with the consent of the Secretary of the Treasury.

''(2) QUALIFIED CHANGE IN METHOD OF ACCOUNTING.—For purposes of this subsection, the term 'qualified change in method of accounting' means any change in method of accounting which—

''(A) is required by the amendments made by this section, or

''(B) was prohibited under the Internal Revenue Code of 1986 prior to such amendments and is permitted under such Code after such amendments.

''(e) SPECIAL RULES FOR ORIGINAL ISSUE DISCOUNT.—Notwithstanding subsection (c), in the case of income from a debt instrument having original issue discount—

''(1) the amendments made by this section shall apply to taxable years beginning after December 31, 2018, and

''(2) the period for taking into account any adjustments under section 481 by reason of a qualified change in method of accounting (as defined in subsection (d)) shall be 6 years.''

EFFECTIVE DATE OF 2015 AMENDMENT

Pub. L. 114–113, div. Q, title I, §191(b), Dec. 18, 2015, 129 Stat. 3075, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2014.''

EFFECTIVE DATE OF 2014 AMENDMENT

Pub. L. 113–295, div. A, title I, §159(b), Dec. 19, 2014, 128 Stat. 4022, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2013.''

EFFECTIVE DATE OF 2013 AMENDMENT

Pub. L. 112–240, title IV, §411(b), Jan. 2, 2013, 126 Stat. 2343, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2011.''

EFFECTIVE DATE OF 2005 AMENDMENT

Pub. L. 109–58, title XIII, §1305(c), Aug. 8, 2005, 119 Stat. 997, provided that:

''(1) IN GENERAL.—The amendment made by subsection (a) [amending this section] shall apply to transactions occurring after the date of the enactment of this Act [Aug. 8, 2005].

''(2) TECHNICAL AMENDMENT.—The amendment made by subsection (b) [amending this section] shall take effect as if included in the amendments made by section 909 of the American Jobs Creation Act of 2004 [Pub. L. 108–357, amending this section].''

EFFECTIVE DATE OF 2010 AMENDMENT

Pub. L. 111–312, title VII, §705(b), Dec. 17, 2010, 124 Stat. 3311, provided that: ''The amendment made by this section [amending this section] shall apply to dispositions after December 31, 2009.''

EFFECTIVE DATE OF 2008 AMENDMENT

Pub. L. 110–343, div. B, title I, §109(d), Oct. 3, 2008, 122 Stat. 3822, provided that:

''(1) EXTENSION.—The amendments made by subsection (a) [amending this section] shall apply to transactions after December 31, 2007.

''(2) TRANSFERS OF OPERATIONAL CONTROL.—The amendment made by subsection (b) [amending this section] shall take effect as if included in section 909 of the American Jobs Creation Act of 2004 [Pub. L. 108–357].

''(3) EXCEPTION FOR PROPERTY LOCATED OUTSIDE THE UNITED STATES.—The amendment made by subsection (c) [amending this section] shall apply to transactions after the date of the enactment of this Act [Oct. 3, 2008].''

EFFECTIVE DATE OF 2004 AMENDMENT

Pub. L. 108–357, title III, §311(d), Oct. 22, 2004, 118 Stat. 1467, provided that: ''The amendments made by this section [amending this section and section 1033 of this title] shall apply to any taxable year with respect to which the due date (without regard to extensions) for the return is after December 31, 2002.''

Pub. L. 108–357, title VIII, §909(b), Oct. 22, 2004, 118 Stat. 1659, provided that: ''The amendments made by this section [amending this section] shall apply to transactions occurring after the date of the enactment of this Act [Oct. 22, 2004], in taxable years ending after such date.''

EFFECTIVE DATE OF 1998 AMENDMENT

Pub. L. 105–277, div. J, title V, §5301(b), Oct. 21, 1998, 112 Stat. 2681–918, provided that:

''(1) IN GENERAL.—The amendment made by this section [amending this section] shall apply to any prize to which a person first becomes entitled after the date of enactment of this Act [Oct. 21, 1998].

''(2) TRANSITION RULE.—The amendment made by this section shall apply to any prize to which a person first becomes entitled on or before the date of enactment of this Act, except that in determining whether an option is a qualified prize option as defined in section 451(h)(2)(A) [now 451(j)(2)(A)] of the Internal Revenue Code of 1986 (as added by such amendment)—

''(A) clause (ii) of such section 451(h)(2)(A) [now 451(j)(2)(A)] shall not apply, and

''(B) such option shall be treated as a qualified prize option if it is exercisable only during all or part of the 18-month period beginning on July 1, 1999.''

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105–34, title IX, §913(c), Aug. 5, 1997, 111 Stat. 878, provided that: ''The amendments made by this section [amending this section and section 1033 of this title] shall apply to sales and exchanges after December 31, 1996.''

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1009(d)(3) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Pub. L. 100–647, title VI, §6030(b), Nov. 10, 1988, 102 Stat. 3694, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to sales or exchanges occurring after December 31, 1987.''

Pub. L. 100–647, title VI, §6033(b), Nov. 10, 1988, 102 Stat. 3695, as amended by Pub. L. 101–239, title VII, §7816(g), Dec. 19, 1989, 103 Stat. 2421, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to payments received before, on, or after the date of enactment of this Act [Nov. 10, 1988].''

EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99–514, title VIII, §821(b), Oct. 22, 1986, 100 Stat. 2373, as amended by Pub. L. 100–647, title I, §1008(h), Nov. 10, 1988, 102 Stat. 3444, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1986.

''(2) CHANGE IN METHOD OF ACCOUNTING.—If a taxpayer is required by the amendments made by this section to change its method of accounting for any taxable year—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as having been made with the consent of the Secretary, and

''(C) the adjustments under section 481 of the Internal Revenue Code of 1954 [now 1986] by reason of such change shall be taken into account ratably over a period no longer than the first 4 taxable years beginning after December 31, 1986.

''(3) SPECIAL RULE FOR CERTAIN CYCLE BILLING.—If a taxpayer for any taxable year beginning before August 16, 1986, for purposes of chapter 1 of the Internal Revenue Code of 1986 took into account income from services described in section 451(f) [now 451(h)] of such Code (as added by subsection (a)) on the basis of the period in which the customers' meters were read, then such treatment for such year shall be deemed to be proper. The preceding sentence shall also apply to any taxable year beginning after August 16, 1986, and before January 1, 1987, if the taxpayer treated such income in the same manner for the taxable year preceding such taxable year.''

Pub. L. 99–514, title IX, §905(c), Oct. 22, 1986, 100 Stat. 2387, as amended by Pub. L. 100–647, title I, §1009(d)(2), Nov. 10, 1988, 102 Stat. 3450, provided that:

''(1) IN GENERAL.—The amendment made by subsection (a) [amending section 165 of this title] shall apply to taxable years beginning after December 31,

1981, and, except as provided in paragraph (2), the amendment made by subsection (b) [amending this section] shall apply to taxable years beginning after December 31, 1982.

''(2) SPECIAL RULES FOR SUBSECTION (b).—

''(A) The amendment made by subsection (b) [amending this section] shall apply to taxable years beginning after December 31, 1982, and before January 1, 1987, only if the qualified individual elects to have such amendment apply for all such taxable years.

''(B) In the case of interest attributable to the period beginning January 1, 1983, and ending December 31, 1987, the interest deduction of financial institutions shall be determined without regard to paragraph (3) of section 451(f) [now 451(h)] of the Internal Revenue Code of 1986 (as added by subsection (b)).''

EFFECTIVE DATE OF 1976 AMENDMENT

Pub. L. 94–455, title XXI, §2102(c), Oct. 4, 1976, 90 Stat. 1900, provided that: ''The amendments made by this section [amending this section] shall apply to payments received after December 31, 1973, in taxable years ending after such date.''

Pub. L. 94–455, title XXI, §2141(b), Oct. 4, 1976, 90 Stat. 1933, provided that: ''The amendment made by this section [amending this section] applies to taxable years beginning after December 31, 1975.''

EFFECTIVE DATE OF 1969 AMENDMENT

Pub. L. 91–172, title II, §215(b), Dec. 30, 1969, 83 Stat. 573, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years ending after the date of the enactment of this Act [Dec. 30, 1969].''

EFFECTIVE DATE OF 1965 AMENDMENT

Amendment by Pub. L. 89–97 applicable only with respect to tips received by employees after 1965, see section 313(f) of Pub. L. 89–97, set out as an Effective Date note under section 6053 of this title.

TAX TREATMENT OF INCENTIVE PAYMENT

Voluntary separation incentives paid to members of Armed Forces under 10 U.S.C. 1175 as includable in gross income only for taxable year in which incentive is paid, see section 662(b) of Pub. L. 102–190, set out as a note under section 1175 of Title 10, Armed Forces.

OVERPAYMENTS OR UNDERPAYMENTS OF TAX ATTRIBUTABLE TO CERTAIN AMENDMENTS BY PUB. L. 99–514 OR PUB. L. 100–647

For provisions relating to credit or refund of overpayments of tax, and assessment of underpayments of tax, due to amendments by section 905 of Pub. L. 99–514 or section 1009(d) of Pub. L. 100–647, see section 1009(d)(4) of Pub. L. 100–647, set out as a note under section 165 of this title.

MODIFICATION OF REGULATIONS ON THE COMPLETED CONTRACT METHOD OF ACCOUNTING

Pub. L. 97–248, title II, §229, Sept. 3, 1982, 96 Stat. 493, as amended by Pub. L. 98–369, div. A, title VII, §712(m), July 18, 1984, 98 Stat. 955, provided that:

''(a) IN GENERAL.—The Secretary of the Treasury shall modify the income tax regulations relating to accounting for long-term contracts to—

''(1) clarify the time at which a contract is to be considered completed,

''(2) clarify when—

''(A) one agreement will be treated as more than one contract, and

''(B) two or more agreements will be treated as one contract, and

''(3) properly allocate all costs which directly benefit, or are incurred by reason of, the extended period long-term contract activities of the taxpayer.

''(b) EXTENDED PERIOD LONG-TERM CONTRACTS DEFINED.—For purposes of this section—

''(1) IN GENERAL.—The term 'extended period long-term contract' means any long-term contract which the taxpayer estimates (at the time such contract is entered into) will not be completed within the 2-year period beginning on the contract commencement date of such contract.

''(2) CERTAIN CONSTRUCTION CONTRACTS.—

''(A) IN GENERAL.—The term 'extended period long-term contract' does not include any construction contract entered into by a taxpayer—

''(i) who estimates (at the time such contract is entered into) that such contract will be completed within the 3-year period beginning on the contract commencement date of such contract, or

''(ii) whose average annual gross receipts over the 3 taxable years preceding the taxable year in which such contract is entered into do not exceed $25,000,000.

''(B) DETERMINATION OF TAXPAYER'S GROSS RECEIPTS.—For purposes of subparagraph (A), the gross receipts of—

''(i) all trades or businesses (whether or not incorporated) which are under common control with the taxpayer (within the meaning of section 52(b)), and

''(ii) all members of any controlled group of corporations of which the taxpayer is a member,

for the 3 taxable years of such persons preceding the taxable year in which the contract described in subparagraph (A) is entered into shall be included in the gross receipts of the taxpayer for the period described in subparagraph (A). The Secretary shall prescribe regulations which provide attribution rules that take into account, in addition to the persons and entities described in the preceding sentence, taxpayers who engage in construction contracts through partnerships, joint ventures, and corporations.

''(C) CONTROLLED GROUP OF CORPORATIONS.—The term 'controlled group of corporations' has the meaning given to such term by section 1563(a), except that—

''(i) 'more than 50 percent' shall be substituted for 'at least 80 percent' each place it appears in section 1563(a)(1), and

''(ii) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

''(3) CONSTRUCTION CONTRACT.—The term 'construction contract' means any contract for the building, construction, reconstruction, or rehabilitation of, or the installation of any integral component to, improvements to real property.

''(4) CONTRACT COMMENCEMENT DATE.—The term 'contract commencement date' means, with respect to any contract, the first date on which any costs (other than costs such as bidding expenses or expenses incurred in connection with negotiating the contract) allocable to such contract are incurred.

''(c) EFFECTIVE DATES; SPECIAL RULES.—

''(1) IN GENERAL.—The modifications to regulations which are required to be made under paragraphs (1) and (2) of subsection (a) shall apply with respect to taxable years ending after December 31, 1982.

''(2) COST ALLOCATION.—

''(A) IN GENERAL.—Any modification to Income Tax Regulation 1.451–3 made under subsection (a)(3) which requires additional costs to be allocated to a contract shall apply only to the applicable percentage of such additional costs incurred in taxable years beginning after December 31, 1982, with respect to contracts entered into after such date.

''(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the applicable percentage shall be determined in accordance with the following table:

''If the taxable year begins in calendar year:	**The applicable percentage is:**
1983	33⅓

"If the taxable year begins in calendar year:	The applicable percentage is:
1984	66⅔
1985 or thereafter	100.

''(3) SPECIAL RULES.—

''(A) TIME OF COMPLETION.—Any contract of a taxpayer which would (but for this paragraph) be treated as having been completed prior to the first taxable year of such taxpayer ending after December 31, 1982, solely by reason of any modification to regulations made under subsection (a)(1), shall be treated as having been completed on the first day of such taxable year.

''(B) AGGREGATION AND SEVERANCE.—Any contract of a taxpayer which would (but for this paragraph) be treated as having been completed prior to the first taxable year of such taxpayer ending after December 31, 1982—

''(i) solely by reason of any modification to regulations made under subsection (a)(2), or

''(ii) solely by reason of any modifications to regulations made under both paragraphs (1) and (2) of subsection (a),

shall be treated as having been completed on the first day after December 31, 1982, on which any contract which was severed from such contract (by reason of the modifications made by subsection (a)(2)) is completed (determined after the application of any modifications to regulations made under subsection (a)(1)).

''(4) UNDERPAYMENTS OF ESTIMATED TAX FOR 1982.—To the extent provided in regulations, no addition to tax shall be made under section 6654 or 6655 of the Internal Revenue Code of 1954 for the taxpayer's first taxable year ending after December 31, 1982, by reason of a long-term contract, but only with respect to installments required to be paid before April 13, 1983.''

PRIVATE DEFERRED COMPENSATION PLANS; TAXABLE YEARS ENDING ON OR AFTER FEBRUARY 1, 1978

Pub. L. 95–600, title I, § 132, Nov. 6, 1978, 92 Stat. 2782, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(a) GENERAL RULE.—The taxable year of inclusion in gross income of any amount covered by a private deferred compensation plan shall be determined in accordance with the principles set forth in regulations, rulings, and judicial decisions relating to deferred compensation which were in effect on February 1, 1978.

''(b) PRIVATE DEFERRED COMPENSATION PLAN DEFINED.—

''(1) IN GENERAL.—For purposes of this section, the term 'private deferred compensation plan' means a plan, agreement, or arrangement—

''(A) where the person for whom the service is performed is not a State (within the meaning of paragraph (1) of section 457(d) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]) and not an organization which is exempt from tax under section 501 of such Code, and

''(B) under which the payment or otherwise making available of compensation is deferred.

''(2) CERTAIN PLANS EXCLUDED.—Paragraph (1) shall not apply to—

''(A) a plan described in section 401(a) of the Internal Revenue Code of 1986 which includes a trust, exempt from tax under section 501(a) of such Code,

''(B) an annuity plan or contract described in section 403 of such Code,

''(C) a qualified bond purchase plan described in section 405(a) of such Code,

''(D) that portion of any plan which consists of a transfer of property described in section 83 (determined without regard to subsection (e) thereof of such Code, and

''(E) that portion of any plan which consists of a trust to which section 402(b) of such Code applies.

''(c) EFFECTIVE DATE.—This section shall apply to taxable years ending on or after February 1, 1978.''

YEAR OF INCLUSION FOR DISASTER OR DEFICIENCY PAYMENTS RECEIVED IN 1978; ELECTION

Pub. L. 95–258, § 1, Apr. 7, 1978, 92 Stat. 195, provided that:

''(a) IN GENERAL.—In the case of a taxpayer reporting on the cash receipts and disbursements method of accounting, if—

''(1)(A) the taxpayer receives in his first taxable year beginning in 1978 payments under the Agricultural Act of 1949, as amended, [see Short Title note set out under section 1421 of Title 7, Agriculture], as a result of—

''(i) the destruction or damage to crops caused by drought, flood, or any other natural disaster, or

''(ii) the inability to plant crops because of such a natural disaster, and

''(B) the taxpayer establishes that, under his practice, income from such crops could have been reported for his last taxable year beginning in 1977, or

''(2)(A) the taxpayer receives in his first taxable year beginning in 1978 deficiency (or 'target price') payments under the Agricultural Act of 1949, as amended, for any 1977 crop, and

''(B) the fifth month of such crop's marketing year ends before December 1, 1977,

then the taxpayer may elect to include such proceeds in income for his last taxable year beginning in 1977.

''(b) MAKING AND EFFECT OF ELECTION—An election under this section for any taxable year shall be made at such time and in such manner as the Secretary of the Treasury may by regulations prescribe and shall apply with respect to all proceeds described in subsection (a) which were received by the taxpayer.''

[§ 452. Repealed. June 15, 1955, ch. 143, § 1(a), 69 Stat. 134]

Section, act Aug. 16, 1954, ch. 736, 68A Stat. 152, related to prepaid income.

EFFECTIVE DATE OF REPEAL

Repeal effective with respect to taxable years beginning after Dec. 31, 1953, and ending after Aug. 16, 1954, see section 3 of act June 15, 1955, set out as an Effective Date of 1955 Amendment note under section 381 of this title.

SAVINGS PROVISION

For provisions concerning increase in tax in any taxable year ending on or before June 15, 1955 by reason of enactment of act June 15, 1955, see section 4 of act June 15, 1955, set out as a note under section 381 of this title.

§ 453. Installment method

(a) General rule

Except as otherwise provided in this section, income from an installment sale shall be taken into account for purposes of this title under the installment method.

(b) Installment sale defined

For purposes of this section—

(1) In general

The term ''installment sale'' means a disposition of property where at least 1 payment is to be received after the close of the taxable year in which the disposition occurs.

(2) Exceptions

The term ''installment sale'' does not include—

(A) Dealer dispositions

Any dealer disposition (as defined in subsection (*l*)).

(B) Inventories of personal property

A disposition of personal property of a kind which is required to be included in the inventory of the taxpayer if on hand at the close of the taxable year.

(c) Installment method defined

For purposes of this section, the term ''installment method'' means a method under which the income recognized for any taxable year from a disposition is that proportion of the payments received in that year which the gross profit (realized or to be realized when payment is completed) bears to the total contract price.

(d) Election out

(1) In general

Subsection (a) shall not apply to any disposition if the taxpayer elects to have subsection (a) not apply to such disposition.

(2) Time and manner for making election

Except as otherwise provided by regulations, an election under paragraph (1) with respect to a disposition may be made only on or before the due date prescribed by law (including extensions) for filing the taxpayer's return of the tax imposed by this chapter for the taxable year in which the disposition occurs. Such an election shall be made in the manner prescribed by regulations.

(3) Election revocable only with consent

An election under paragraph (1) with respect to any disposition may be revoked only with the consent of the Secretary.

(e) Second dispositions by related persons

(1) In general

If—

(A) any person disposes of property to a related person (hereinafter in this subsection referred to as the ''first disposition''), and

(B) before the person making the first disposition receives all payments with respect to such disposition, the related person disposes of the property (hereinafter in this subsection referred to as the ''second disposition''),

then, for purposes of this section, the amount realized with respect to such second disposition shall be treated as received at the time of the second disposition by the person making the first disposition.

(2) 2-year cutoff for property other than marketable securities

(A) In general

Except in the case of marketable securities, paragraph (1) shall apply only if the date of the second disposition is not more than 2 years after the date of the first disposition.

(B) Substantial diminishing of risk of ownership

The running of the 2-year period set forth in subparagraph (A) shall be suspended with respect to any property for any period during which the related person's risk of loss with respect to the property is substantially diminished by—

(i) the holding of a put with respect to such property (or similar property),

(ii) the holding by another person of a right to acquire the property, or

(iii) a short sale or any other transaction.

(3) Limitation on amount treated as received

The amount treated for any taxable year as received by the person making the first disposition by reason of paragraph (1) shall not exceed the excess of—

(A) the lesser of—

(i) the total amount realized with respect to any second disposition of the property occurring before the close of the taxable year, or

(ii) the total contract price for the first disposition, over

(B) the sum of—

(i) the aggregate amount of payments received with respect to the first disposition before the close of such year, plus

(ii) the aggregate amount treated as received with respect to the first disposition for prior taxable years by reason of this subsection.

(4) Fair market value where disposition is not sale or exchange

For purposes of this subsection, if the second disposition is not a sale or exchange, an amount equal to the fair market value of the property disposed of shall be substituted for the amount realized.

(5) Later payments treated as receipt of tax paid amounts

If paragraph (1) applies for any taxable year, payments received in subsequent taxable years by the person making the first disposition shall not be treated as the receipt of payments with respect to the first disposition to the extent that the aggregate of such payments does not exceed the amount treated as received by reason of paragraph (1).

(6) Exception for certain dispositions

For purposes of this subsection—

(A) Reacquisitions of stock by issuing corporation not treated as first dispositions

Any sale or exchange of stock to the issuing corporation shall not be treated as a first disposition.

(B) Involuntary conversions not treated as second dispositions

A compulsory or involuntary conversion (within the meaning of section 1033) and any transfer thereafter shall not be treated as a second disposition if the first disposition occurred before the threat or imminence of the conversion.

(C) Dispositions after death

Any transfer after the earlier of—

(i) the death of the person making the first disposition, or

(ii) the death of the person acquiring the property in the first disposition,

and any transfer thereafter shall not be treated as a second disposition.

(7) Exception where tax avoidance not a principal purpose

This subsection shall not apply to a second disposition (and any transfer thereafter) if it is established to the satisfaction of the Secretary that neither the first disposition nor the second disposition had as one of its principal purposes the avoidance of Federal income tax.

(8) Extension of statute of limitations

The period for assessing a deficiency with respect to a first disposition (to the extent such deficiency is attributable to the application of this subsection) shall not expire before the day which is 2 years after the date on which the person making the first disposition furnishes (in such manner as the Secretary may by regulations prescribe) a notice that there was a second disposition of the property to which this subsection may have applied. Such deficiency may be assessed notwithstanding the provisions of any law or rule of law which would otherwise prevent such assessment.

(f) Definitions and special rules

For purposes of this section—

(1) Related person

Except for purposes of subsections (g) and (h), the term ''related person'' means—

(A) a person whose stock would be attributed under section 318(a) (other than paragraph (4) thereof) to the person first disposing of the property, or

(B) a person who bears a relationship described in section 267(b) to the person first disposing of the property.

(2) Marketable securities

The term ''marketable securities'' means any security for which, as of the date of the disposition, there was a market on an established securities market or otherwise.

(3) Payment

Except as provided in paragraph (4), the term ''payment'' does not include the receipt of evidences of indebtedness of the person acquiring the property (whether or not payment of such indebtedness is guaranteed by another person).

(4) Purchaser evidences of indebtedness payable on demand or readily tradable

Receipt of a bond or other evidence of indebtedness which—

(A) is payable on demand, or

(B) is readily tradable,

shall be treated as receipt of payment.

(5) Readily tradable defined

For purposes of paragraph (4), the term ''readily tradable'' means a bond or other evidence of indebtedness which is issued—

(A) with interest coupons attached or in registered form (other than one in registered form which the taxpayer establishes will not be readily tradable in an established securities market), or

(B) in any other form designed to render such bond or other evidence of indebtedness readily tradable in an established securities market.

(6) Like-kind exchanges

In the case of any exchange described in section 1031(b)—

(A) the total contract price shall be reduced to take into account the amount of any property permitted to be received in such exchange without recognition of gain,

(B) the gross profit from such exchange shall be reduced to take into account any amount not recognized by reason of section 1031(b), and

(C) the term ''payment'', when used in any provision of this section other than subsection (b)(1), shall not include any property permitted to be received in such exchange without recognition of gain.

Similar rules shall apply in the case of an exchange which is described in section 356(a) and is not treated as a dividend.

(7) Depreciable property

The term ''depreciable property'' means property of a character which (in the hands of the transferee) is subject to the allowance for depreciation provided in section 167.

(8) Payments to be received defined

The term ''payments to be received'' includes—

(A) the aggregate amount of all payments which are not contingent as to amount, and

(B) the fair market value of any payments which are contingent as to amount.

(g) Sale of depreciable property to controlled entity

(1) In general

In the case of an installment sale of depreciable property between related persons—

(A) subsection (a) shall not apply,

(B) for purposes of this title—

(i) except as provided in clause (ii), all payments to be received shall be treated as received in the year of the disposition, and

(ii) in the case of any payments which are contingent as to the amount but with respect to which the fair market value may not be reasonably ascertained, the basis shall be recovered ratably, and

(C) the purchaser may not increase the basis of any property acquired in such sale by any amount before the time such amount is includible in the gross income of the seller.

(2) Exception where tax avoidance not a principal purpose

Paragraph (1) shall not apply if it is established to the satisfaction of the Secretary that the disposition did not have as one of its principal purposes the avoidance of Federal income tax.

(3) Related persons

For purposes of this subsection, the term ''related persons'' has the meaning given to such term by section 1239(b), except that such term shall include 2 or more partnerships having a relationship to each other described in section 707(b)(1)(B).

(h) Use of installment method by shareholders in certain liquidations

(1) Receipt of obligations not treated as receipt of payment

(A) In general

If, in a liquidation to which section 331 applies, the shareholder receives (in exchange for the shareholder's stock) an installment obligation acquired in respect of a sale or exchange by the corporation during the 12-month period beginning on the date a plan of complete liquidation is adopted and the liquidation is completed during such 12-month period, then, for purposes of this section, the receipt of payments under such obligation (but not the receipt of such obligation) by the shareholder shall be treated as the receipt of payment for the stock.

(B) Obligations attributable to sale of inventory must result from bulk sale

Subparagraph (A) shall not apply to an installment obligation acquired in respect of a sale or exchange of—

(i) stock in trade of the corporation,

(ii) other property of a kind which would properly be included in the inventory of the corporation if on hand at the close of the taxable year, and

(iii) property held by the corporation primarily for sale to customers in the ordinary course of its trade or business,

unless such sale or exchange is to 1 person in 1 transaction and involves substantially all of such property attributable to a trade or business of the corporation.

(C) Special rule where obligor and shareholder are related persons

If the obligor of any installment obligation and the shareholder are married to each other or are related persons (within the meaning of section 1239(b)), to the extent such installment obligation is attributable to the disposition by the corporation of depreciable property—

(i) subparagraph (A) shall not apply to such obligation, and

(ii) for purposes of this title, all payments to be received by the shareholder shall be deemed received in the year the shareholder receives the obligation.

(D) Coordination with subsection (e)(1)(A)

For purposes of subsection (e)(1)(A), disposition of property by the corporation shall be treated also as disposition of such property by the shareholder.

(E) Sales by liquidating subsidiaries

For purposes of subparagraph (A), in the case of a controlling corporate shareholder (within the meaning of section 368(c)) of a selling corporation, an obligation acquired in respect of a sale or exchange by the selling corporation shall be treated as so acquired by such controlling corporate shareholder. The preceding sentence shall be applied successively to each controlling corporate shareholder above such controlling corporate shareholder.

(2) Distributions received in more than 1 taxable year of shareholder

If—

(A) paragraph (1) applies with respect to any installment obligation received by a shareholder from a corporation, and

(B) by reason of the liquidation such shareholder receives property in more than 1 taxable year,

then, on completion of the liquidation, basis previously allocated to property so received shall be reallocated for all such taxable years so that the shareholder's basis in the stock of the corporation is properly allocated among all property received by such shareholder in such liquidation.

(i) Recognition of recapture income in year of disposition

(1) In general

In the case of any installment sale of property to which subsection (a) applies—

(A) notwithstanding subsection (a), any recapture income shall be recognized in the year of the disposition, and

(B) any gain in excess of the recapture income shall be taken into account under the installment method.

(2) Recapture income

For purposes of paragraph (1), the term ''recapture income'' means, with respect to any installment sale, the aggregate amount which would be treated as ordinary income under section 1245 or 1250 (or so much of section 751 as relates to section 1245 or 1250) for the taxable year of the disposition if all payments to be received were received in the taxable year of disposition.

(j) Regulations

(1) In general

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the provisions of this section.

(2) Selling price not readily ascertainable

The regulations prescribed under paragraph (1) shall include regulations providing for ratable basis recovery in transactions where the gross profit or the total contract price (or both) cannot be readily ascertained.

(k) Current inclusion in case of revolving credit plans, etc.

In the case of—

(1) any disposition of personal property under a revolving credit plan, or

(2) any installment obligation arising out of a sale of—

(A) stock or securities which are traded on an established securities market, or

(B) to the extent provided in regulations, property (other than stock or securities) of a kind regularly traded on an established market,

subsection (a) shall not apply, and, for purposes of this title, all payments to be received shall be treated as received in the year of disposition. The Secretary may provide for the application of this subsection in whole or in part for trans-

actions in which the rules of this subsection otherwise would be avoided through the use of related parties, pass-thru entities, or intermediaries.

(*l*) Dealer dispositions

For purposes of subsection (b)(2)(A)—

(1) In general

The term ''dealer disposition'' means any of the following dispositions:

(A) Personal property

Any disposition of personal property by a person who regularly sells or otherwise disposes of personal property of the same type on the installment plan.

(B) Real property

Any disposition of real property which is held by the taxpayer for sale to customers in the ordinary course of the taxpayer's trade or business.

(2) Exceptions

The term ''dealer disposition'' does not include—

(A) Farm property

The disposition on the installment plan of any property used or produced in the trade or business of farming (within the meaning of section 2032A(e)(4) or (5)).

(B) Timeshares and residential lots

(i) In general

Any dispositions described in clause (ii) on the installment plan if the taxpayer elects to have paragraph (3) apply to any installment obligations which arise from such dispositions. An election under this paragraph shall not apply with respect to an installment obligation which is guaranteed by any person other than an individual.

(ii) Dispositions to which subparagraph applies

A disposition is described in this clause if it is a disposition in the ordinary course of the taxpayer's trade or business to an individual of—

(I) a timeshare right to use or a timeshare ownership interest in residential real property for not more than 6 weeks per year, or a right to use specified campgrounds for recreational purposes, or

(II) any residential lot, but only if the taxpayer (or any related person) is not to make any improvements with respect to such lot.

For purposes of subclause (I), a timeshare right to use (or timeshare ownership interest in) property held by the spouse, children, grandchildren, or parents of an individual shall be treated as held by such individual.

(C) Carrying charges or interest

Any carrying charges or interest with respect to a disposition described in subparagraph (A) or (B) which are added on the books of account of the seller to the established cash selling price of the property shall be included in the total contract price of the property and, if such charges or interest are not so included, any payments received shall be treated as applying first against such carrying charges or interest.

(3) Payment of interest on timeshares and residential lots

(A) In general

In the case of any installment obligation to which paragraph (2)(B) applies, the tax imposed by this chapter for any taxable year for which payment is received on such obligation shall be increased by the amount of interest determined in the manner provided under subparagraph (B).

(B) Computation of interest

(i) In general

The amount of interest referred to in subparagraph (A) for any taxable year shall be determined—

(I) on the amount of the tax for such taxable year which is attributable to the payments received during such taxable year on installment obligations to which this subsection applies,

(II) for the period beginning on the date of sale, and ending on the date such payment is received, and

(III) by using the applicable Federal rate under section 1274 (without regard to subsection (d)(2) thereof) in effect at the time of the sale compounded semiannually.

(ii) Interest not taken into account

For purposes of clause (i), the portion of any tax attributable to the receipt of any payment shall be determined without regard to any interest imposed under subparagraph (A).

(iii) Taxable year of sale

No interest shall be determined for any payment received in the taxable year of the disposition from which the installment obligation arises.

(C) Treatment as interest

Any amount payable under this paragraph shall be taken into account in computing the amount of any deduction allowable to the taxpayer for interest paid or accrued during such taxable year.

(Added Pub. L. 96–471, § 2(a), Oct. 19, 1980, 94 Stat. 2247; amended Pub. L. 97–34, title II, § 202(c), Aug. 13, 1981, 95 Stat. 221; Pub. L. 97–448, title III, § 303, Jan. 12, 1983, 96 Stat. 2398; Pub. L. 98–369, div. A, title I, § 112(a), title IV, § 421(b)(6)(B), (C), July 18, 1984, 98 Stat. 635, 794; Pub. L. 99–514, title VI, §§ 631(e)(8), 642(a)(1)(D), (3), (b), title VIII, § 812(a), title XVIII, § 1809(c), Oct. 22, 1986, 100 Stat. 2274, 2284, 2371, 2821; Pub. L. 100–203, title X, § 10202(b), Dec. 22, 1987, 101 Stat. 1330–388; Pub. L. 100–647, title I, §§ 1006(e)(7), (i)(1), (2), 1008(g)(1), 1018(u)(25), (26), title II, § 2004(d)(1), (5), Nov. 10, 1988, 102 Stat. 3401, 3410, 3442, 3591, 3599; Pub. L. 106–170, title V, § 536(a), Dec. 17, 1999, 113 Stat. 1936; Pub. L. 106–573, § 2(a), Dec. 28, 2000, 114 Stat.

3061; Pub. L. 108–357, title VIII, §897(a), Oct. 22, 2004, 118 Stat. 1649.)

PRIOR PROVISIONS

A prior section 453, acts Aug. 16, 1954, ch. 736, 68A Stat. 154; Sept. 2, 1958, Pub. L. 85–866, title I, §27(a), 72 Stat. 1624; Oct. 16, 1962, Pub. L. 87–834, §13(f)(5), 76 Stat. 1035; Feb. 26, 1964, Pub. L. 88–272, title II, §§222(a), 231(b)(5), 78 Stat. 75, 105; Aug. 22, 1964, Pub. L. 88–484, §1(b)(2), 78 Stat. 597; Aug. 31, 1964, Pub. L. 88–539, §3(a), (b), 78 Stat. 746; Sept. 12, 1966, Pub. L. 89–570, §1(b)(5), 80 Stat. 762; Nov. 13, 1966, Pub. L. 89–809, title II, §202(c), 80 Stat. 1576; Dec. 30, 1969, Pub. L. 91–172, title II, §211(b)(5), title III, §301(b)(7), title IV, §412(a), title IX, §916(a), 83 Stat. 570, 585, 608, 723; Oct. 4, 1976, Pub. L. 94–455, title II, §205(c)(1)(E), title XIX, §§1901(a)(66), 1906(b)(13)(A), 1951(b)(7)(A), 90 Stat. 1535, 1775, 1834, 1838; Nov. 6, 1978, Pub. L. 95–600, title VII, §703(j)(3), 92 Stat. 2941; Apr. 1, 1980, Pub. L. 96–222, title I, §104(a)(4)(H)(iv), 94 Stat. 217; Apr. 2, 1980, Pub. L. 96–223, title IV, §403(b)(2)(B), 94 Stat. 305; Oct. 19, 1980, Pub. L. 96–471, §2(c)(4), 94 Stat. 2254, related to installment method in general, installment method for dealers in personal property, and gain or loss dispositions of installment obligations, prior to repeal by Pub. L. 96–471, §2(a), Oct. 19, 1980, 94 Stat. 2247. See sections 453A and 453B of this title.

AMENDMENTS

2004—Subsec. (f)(4)(B). Pub. L. 108–357 struck out ''is issued by a corporation or a government or political subdivision thereof and'' before ''is readily tradable''.

2000—Subsecs. (a), (d)(1), (i)(1), (k). Pub. L. 106–573 repealed Pub. L. 106–170, §536(a). See 1999 Amendment notes below.

1999—Subsec. (a). Pub. L. 106–170, §536(a)(1), which substituted ''Use of installment method'' for ''General rule'' in subsec. heading, designated existing provisions as par. (1) and inserted heading, and added heading and text of par. (2), text of which read as follows: ''(2) ACCRUAL METHOD TAXPAYER.—The installment method shall not apply to income from an installment sale if such income would be reported under an accrual method of accounting without regard to this section. The preceding sentence shall not apply to a disposition described in subparagraph (A) or (B) of subsection (*l*)(2).'', was repealed by Pub. L. 106–573, §2(a). See Effective Date and Construction of 2000 Amendment note below.

Subsecs. (d)(1), (i)(1), (k). Pub. L. 106–170, §536(a)(2), which substituted ''(a)(1)'' for ''(a)'' wherever appearing, was repealed by Pub. L. 106–573. See Effective Date and Construction of 2000 Amendment note below.

1988—Subsec. (f)(1). Pub. L. 100–647, §1018(u)(25), substituted ''subsections (g)'' for ''subsection (g)''.

Subsec. (f)(8). Pub. L. 100–647, §1018(u)(26), substituted ''payments to be'' for ''payment to be''.

Subsec. (g)(1). Pub. L. 100–647, §1006(i)(2)(B), struck out ''(within the meaning of section 1239(b))'' after ''between related persons''.

Pub. L. 100–647, §1006(i)(1), added subpars. (A) to (C) and struck out former subpars. (A) and (B) which read as follows:

''(A) subsection (a) shall not apply, and

''(B) for purposes of this title—

''(i) except as provided in clause (ii), all payments to be received shall be treated as received in the year of the disposition, and

''(ii) in the case of any payments which are contingent as to amount but with respect to which the fair market value may not be reasonably ascertained—

''(I) the basis shall be recovered ratably, and

''(II) the purchaser may not increase the basis of any property acquired in such sale by any amount before such time as the seller includes such amount in income.''

Subsec. (g)(3). Pub. L. 100–647, §1006(i)(2)(A), added par. (3).

Subsec. (h)(1)(B). Pub. L. 100–647, §1006(e)(7)(A), substituted ''to 1 person in 1 transaction'' for ''to one person'' in concluding provisions.

Subsec. (h)(1)(E). Pub. L. 100–647, §1006(e)(7)(B), substituted ''section 368(c)'' for ''section 368(c)(1)''.

Subsec. (j). Pub. L. 100–647, §1008(g)(1), redesignated subsec. (j), relating to current inclusion in case of revolving credit plans, etc., as (k).

Subsec. (k). Pub. L. 100–647, §2004(d)(5), struck out ''and section 453A'' after ''subsection (a)'' in second sentence.

Pub. L. 100–647, §1008(g)(1), redesignated subsec. (j), relating to current inclusion in case of revolving credit plans, etc., as (k).

Subsec. (*l*)(1)(A). Pub. L. 100–647, §2004(d)(1), inserted ''of the same type'' after ''disposes of personal property''.

1987—Subsec. (b)(2)(A). Pub. L. 100–203, §10202(b)(1), substituted ''Dealer dispositions'' for ''Dealer disposition of personal property'' in heading and amended text generally. Prior to amendment, text read as follows: ''A disposition of personal property on the installment plan by a person who regularly sells or otherwise disposes of personal property on the installment plan.''

Subsec. (*l*). Pub. L. 100–203, §10202(b)(2), added subsec. (*l*).

1986—Subsec. (f)(1). Pub. L. 99–514, §642(a)(3), amended par. (1) generally. Prior to amendment, par. (1) read as follows: ''Except for purposes of subsections (g) and (h), the term 'related person' means a person whose stock would be attributed under section 318(a) (other than paragraph (4) thereof) to the person first disposing of the property.''

Subsec. (f)(8). Pub. L. 99–514, §642(b)(1), added par. (8).

Subsec. (g). Pub. L. 99–514, §642(a)(1)(D), substituted ''controlled entity'' for ''80-percent owned entity'' in heading.

Subsec. (g)(1). Pub. L. 99–514, §642(b)(2), amended par. (1) generally. Prior to amendment, par. (1) read as follows: ''In the case of an installment sale of depreciable property between related persons within the meaning of section 1239(b), subsection (a) shall not apply, and, for purposes of this title, all payments to be received shall be deemed received in the year of the disposition.''

Subsec. (h). Pub. L. 99–514, §631(e)(8)(C), substituted ''certain liquidations'' for ''section 337 liquidations'' in heading.

Subsec. (h)(1)(A). Pub. L. 99–514, §631(e)(8)(A), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''If, in connection with a liquidation to which section 337 applies, in a transaction to which section 331 applies the shareholder receives (in exchange for the shareholder's stock) an installment obligation acquired in respect of a sale or exchange by the corporation during the 12-month period set forth in section 337(a), then, for purposes of this section, the receipt of payments under such obligation (but not the receipt of such obligation) by the shareholder shall be treated as the receipt of payment for the stock.''

Subsec. (h)(1)(B). Pub. L. 99–514, §631(e)(8)(A), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: ''Subparagraph (A) shall not apply to an installment obligation described in section 337(b)(1)(B) unless such obligation is also described in section 337(b)(2)(B).''

Subsec. (h)(1)(E). Pub. L. 99–514, §631(e)(8)(B), substituted ''subsidiaries'' for ''subsidiary'' in heading and amended text generally. Prior to amendment, subpar. (E) read as follows: ''For purposes of subparagraph (A), in any case to which section 337(c)(3) applies, an obligation acquired in respect of a sale or exchange by the selling corporation shall be treated as so acquired by the corporation distributing the obligation to the shareholder.''

Subsec. (i)(2). Pub. L. 99–514, §1809(c), substituted ''section 1245 or 1250 (or so much of section 751 as relates to section 1245 or 1250)'' for ''section 1245 or 1250''.

Subsec. (j). Pub. L. 99–514, §812(a), added subsec. (j) relating to current inclusion in case of revolving credit plans, etc.

1984—Subsec. (g). Pub. L. 98–369, §421(b)(6)(C), struck out ''spouse or'' after ''property to'' in heading.

Subsec. (h)(1)(C). Pub. L. 98–369, § 421(b)(6)(B), inserted ''married to each other or are''.

Subsec. (i). Pub. L. 98–369, § 112(a), amended subsec. (i) generally, substituting provisions relating to recognition of recapture income in year of disposition for provisions relating to application of subsec. (a) in the case of an installment sale of section 179 property.

1983—Subsec. (f)(6)(C). Pub. L. 97–448 inserted '', when used in any provision of this section other than subsection (b)(1),'' after ''the term 'payment' ''.

1981—Subsecs. (i), (j). Pub. L. 97–34 added subsec. (i) and redesignated former subsec. (i) as (j).

EFFECTIVE DATE OF 2004 AMENDMENT

Pub. L. 108–357, title VIII, § 897(b), Oct. 22, 2004, 118 Stat. 1649, provided that: ''The amendment made by this section [amending this section] shall apply to sales occurring on or after the date of the enactment of this Act [Oct. 22, 2004].''

EFFECTIVE DATE AND CONSTRUCTION OF 2000 AMENDMENT

Pub. L. 106–573, § 2, Dec. 28, 2000, 114 Stat. 3061, provided that:

''(a) IN GENERAL.—Subsection (a) of section 536 of the Ticket to Work and Work Incentives Improvement Act of 1999 (relating to modification of installment method and repeal of installment method for accrual method taxpayers) [Pub. L. 106–170, amending this section] is repealed effective with respect to sales and other dispositions occurring on or after the date of the enactment of such Act [Dec. 17, 1999].

''(b) APPLICABILITY.—The Internal Revenue Code of 1986 shall be applied and administered as if that subsection (and the amendments made by that subsection) had not been enacted.''

EFFECTIVE DATE OF 1999 AMENDMENT

Pub. L. 106–170, title V, § 536(c), Dec. 17, 1999, 113 Stat. 1936, provided that: ''The amendments made by this section [amending this section and section 453A of this title] shall apply to sales or other dispositions occurring on or after the date of the enactment of this Act [Dec. 17, 1999].''

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by sections 1006(e)(7), (i)(1), (2), 1008(g)(1), and 1018(u)(25), (26) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Amendment by section 2004(d)(1), (5) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provisions of the Revenue Act of 1987, Pub. L. 100–203, title X, to which such amendment relates, see section 2004(u) of Pub. L. 100–647, set out as a note under section 56 of this title.

EFFECTIVE DATE OF 1987 AMENDMENT

Pub. L. 100–203, title X, § 10202(e), Dec. 22, 1987, 101 Stat. 1330–392, as amended by Pub. L. 100–647, title II, § 2004(d)(3), (4), (6), Nov. 10, 1988, 102 Stat. 3599, 3600, provided that:

''(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [amending this section and sections 56, 381, 453A, and 691 of this title and repealing section 453C of this title] shall apply to dispositions in taxable years beginning after December 31, 1987.

''(2) SPECIAL RULES FOR DEALERS.—

''(A) IN GENERAL.—In the case of dealer dispositions (within the meaning of section 453(*l*)(1) of the Internal Revenue Code of 1986 as added by this section), the amendments made by subsections (a) and (b) [amending this section and repealing section 453C of this title] shall apply to installment obligations arising from dispositions after December 31, 1987.

''(B) SPECIAL RULES FOR OBLIGATIONS ARISING FROM DEALER DISPOSITIONS AFTER FEBRUARY 28, 1986, AND BEFORE JANUARY 1, 1988.—

''(i) IN GENERAL.—In the case of an applicable installment obligation arising from a disposition described in subclause (I) or (II) of section 453C(e)(1)(A)(i) of the Internal Revenue Code of 1986 (as in effect before the amendments made by this section) before January 1, 1988, the amendments made by subsections (a) and (b) shall apply to taxable years beginning after December 31, 1987.

''(ii) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer who is required by clause (i) to change its method of accounting for any taxable year with respect to obligations described in clause (i)—

''(I) such change shall be treated as initiated by the taxpayer,

''(II) such change shall be treated as made with the consent of the Secretary of the Treasury or his delegate, and

''(III) the net amount of adjustments required by section 481 of the Internal Revenue Code of 1986 shall be taken into account over a period not longer than 4 taxable years.

''(C) CERTAIN RULES MADE APPLICABLE.—For purposes of this paragraph, rules similar to the rules of paragraphs (4) and (5) of section 812(c) of the Tax Reform Act of 1986 [Pub. L. 99–514, set out as an Effective Date of 1986 Amendment note below] (as added by the Technical and Miscellaneous Revenue Act of 1988 [Pub. L. 100–647]) shall apply.

''(3) SPECIAL RULE FOR NONDEALERS.—

''(A) ELECTION.—A taxpayer may elect, at such time and in such manner as the Secretary of the Treasury or his delegate may prescribe, to have the amendments made by subsections (a) and (c) [amending sections 381, 453A, and 691 of this title and repealing section 453C of this title] apply to taxable years ending after December 31, 1986, with respect to dispositions and pledges occurring after August 16, 1986.

''(B) PLEDGING RULES.—Except as provided in subparagraph (A)—

''(i) IN GENERAL.—Section 453A(d) of the Internal Revenue Code of 1986 shall apply to any installment obligation which is pledged to secure any secured indebtedness (within the meaning of section 453A(d)(4) of such Code) after December 17, 1987, in taxable years ending after such date.

''(ii) COORDINATION WITH SECTION 453C.—For purposes of section 453C of such Code (as in effect before its repeal), the face amount of any obligation to which section 453A(d) of such Code applies shall be reduced by the amount treated as payments on such obligation under section 453A(d) of such Code and the amount of any indebtedness secured by it shall not be taken into account.

''(C) CERTAIN DISPOSITIONS DEEMED MADE ON 1ST DAY OF TAXABLE YEAR.—If the taxpayer makes an election under subparagraph (A), in the case of the taxpayer's 1st taxable year ending after December 31, 1986—

''(i) dispositions after August 16, 1986, and before the 1st day of such taxable year shall be treated as made on such 1st day, and

''(ii) subsections (b)(2)(B) and (c)(4) of section 453A of such Code shall be applied separately with respect to such dispositions by substituting for '$5,000,000' the amount which bears the same ratio to $5,000,000 as the number of days after August 16, 1986, and before such 1st day bears to 365.

''(4) MINIMUM TAX.—The amendment made by subsection (d) [amending section 56 of this title] shall apply to dispositions in taxable years beginning after December 31, 1986.

''(5) COORDINATION WITH TAX REFORM ACT OF 1986.—The amendments made by this section shall not apply to any installment obligation or to any taxpayer during any period to the extent the amendments made by section 811 of the Tax Reform Act of 1986 [section 811 of Pub. L. 99–514, amending former section 453C of this title and enacting provisions set out as a note under former section 453C of this title] do not apply to such obligation or during such period.''

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 631(e)(8) of Pub. L. 99–514 applicable to any distribution in complete liquidation, and any sale or exchange, made by a corporation after July 31, 1986, unless such corporation is completely liquidated before Jan. 1, 1987, any transaction described in section 338 of this title for which the acquisition date occurs after Dec. 31, 1986, and any distribution, not in complete liquidation, made after Dec. 31, 1986, with exceptions and special and transitional rules, see section 633 of Pub. L. 99–514, set out as an Effective Date note under section 336 of this title.

Amendment by section 642(a)(1)(D), (3), (b) of Pub. L. 99–514 applicable to sales after Oct. 22, 1986, in taxable years ending after such date, but not applicable to sales made after Aug. 14, 1986, which are made pursuant to a binding contract in effect on Aug. 14, 1986, and at all times thereafter, see section 642(c) of Pub. L. 99–514, set out as a note under section 1239 of this title.

Pub. L. 99–514, title VIII, §812(c), Oct. 22, 1986, 100 Stat. 2372, as amended by Pub. L. 100–647, title I, §1008(g)(3)–(6), Nov. 10, 1988, 102 Stat. 3443, provided that:

''(1) IN GENERAL.—Except as provided in paragraphs (2) and (3), the amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1986.

''(2) SALES OF STOCK, ETC.—Section 453(k)(2) of the Internal Revenue Code of 1986, as added by subsection (a), shall apply to sales after December 31, 1986, in taxable years ending after such date.

''(3) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer who made sales under a revolving credit plan and was on the installment method under section 453 or 453A of the Internal Revenue Code of 1986 for such taxpayer's last taxable year beginning before January 1, 1987, the amendments made by this section [amending this section and section 453A of this title] shall be treated as a change in method of accounting for its 1st taxable year beginning after December 31, 1986, and—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as having been made with the consent of the Secretary,

''(C) the period for taking into account adjustments under section 481 of such Code by reason of such change shall be equal to 4 years, and

''(D) except as provided in paragraph (4), the amount taken into account in each of such 4 years shall be the applicable percentage (determined in accordance with the following table) of the net adjustment:

"In the case of the:	**The applicable percentage is:**
1st taxable year	15
2nd taxable year	25
3rd taxable year	30
4th taxable year	30.

If the taxpayer's last taxable year beginning before January 1, 1987, was the taxpayer's 1st taxable year in which sales were made under a revolving credit plan, all adjustments under section 481 of such Code shall be taken into account in the taxpayer's 1st taxable year beginning after December 31, 1986.

''(4) ACCELERATION OF ADJUSTMENTS WHERE CONTRACTION IN AMOUNT OF INSTALLMENT OBLIGATIONS.—

''(A) IN GENERAL.—If the percentage determined under subparagraph (B) for any taxable year in the adjustment period exceeds the percentage which would otherwise apply under paragraph (3)(D) for such taxable year (determined after the application of this paragraph for prior taxable years in the adjustment period)—

''(i) the percentage determined under subparagraph (B) shall be substituted for the applicable percentage which would otherwise apply under paragraph (3)(D), and

''(ii) any increase in the applicable percentage by reason of clause (i) shall be applied to reduce the applicable percentage determined under paragraph (3)(D) for subsequent taxable years in the adjustment period (beginning with the 1st of such subsequent taxable years).

''(B) DETERMINATION OF PERCENTAGE.—For purposes of subparagraph (A), the percentage determined under this subparagraph for any taxable year in the adjustment period is the excess (if any) of—

''(i) the percentage determined by dividing the aggregate contraction in revolving installment obligations by the aggregate face amount of such obligations outstanding as of the close of the taxpayer's last taxable year beginning before January 1, 1987, over

''(ii) the sum of the applicable percentages under paragraph (3)(D) (as modified by this paragraph) for prior taxable years in the adjustment period.

''(C) AGGREGATE CONTRACTION IN REVOLVING INSTALLMENT OBLIGATIONS.—For purposes of subparagraph (B), the aggregate contraction in revolving installment obligations is the amount by which—

''(i) the aggregate face amount of the revolving installment obligations outstanding as of the close of the taxpayer's last taxable year beginning before January 1, 1987, exceeds

''(ii) the aggregate face amount of the revolving installment obligations outstanding as of the close of the taxable year involved.

''(D) REVOLVING INSTALLMENT OBLIGATIONS.—For purposes of this paragraph, the term 'revolving installment obligations' means installment obligations arising under a revolving credit plan.

''(E) TREATMENT OF CERTAIN OBLIGATIONS DISPOSED OF ON OR BEFORE OCTOBER 26, 1987.—For purposes of subparagraphs (B)(i) and (C)(i), in determining the aggregate face amount of revolving installment obligations outstanding as of the close of the taxpayer's last taxable year beginning before January 1, 1987, there shall not be taken into account any obligation—

''(i) which was disposed of to an unrelated person on or before October 26, 1987, or

''(ii) was disposed of to an unrelated person on or after such date pursuant to a binding written contract in effect on October 26, 1987, and at all times thereafter before such disposition.

For purposes of the preceding sentence, the term 'unrelated person' means any person who is not a related person (as defined in section 453(g) of the Internal Revenue Code of 1986).

''(5) LIMITATION ON LOSSES FROM SALES OF OBLIGATIONS UNDER REVOLVING CREDIT PLANS.—If 1 or more obligations arising under a revolving credit plan and taken into account under paragraph (3) are disposed of during the adjustment period, then, notwithstanding any other provision of law—

''(A) no losses from such dispositions shall be recognized, and

''(B) the aggregate amount of the adjustment for taxable years in the adjustment period (in reverse order of time) shall be reduced by the amount of such losses.

''(6) ADJUSTMENT PERIOD.—For purposes of paragraphs (4) and (5), the adjustment period is the 4-year period under paragraph (3).''

Amendment by section 1809(c) of Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Pub. L. 98–369, div. A, title I, §112(b), July 18, 1984, 98 Stat. 635, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [amending this section] shall apply with respect to dispositions made after June 6, 1984.

''(2) EXCEPTION.—The amendments made by this section shall not apply with respect to any disposition conducted pursuant to a contract which was binding on March 22, 1984, and at all times thereafter.

''(3) SPECIAL RULE FOR CERTAIN DISPOSITIONS BEFORE OCTOBER 1, 1984.—The amendments made by this section shall not apply to any disposition before October 1, 1984, of all or substantially all of the personal property of a cable television business pursuant to a written offer delivered by the seller on June 20, 1984, but only if the last payment under the installment contract is due no later than October 1, 1989.''

Amendment by section 421(b)(6)(B), (C) of Pub. L. 98–369 applicable to transfers after July 18, 1984, in taxable years ending after such date, subject to election to have amendment apply to transfers after 1983 or to transfers pursuant to existing decrees, see section 421(d) of Pub. L. 98–369, set out as an Effective Date note under section 1041 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Pub. L. 97–448, title III, § 311(a), Jan. 12, 1983, 96 Stat. 2411, provided that: ''The amendments made by sections 301, 302, and 303 [amending this section and sections 453B and 1239 of this title] shall apply to dispositions made after October 19, 1980, in taxable years ending after such date.''

EFFECTIVE DATE OF 1981 AMENDMENT

Amendment by Pub. L. 97–34 applicable to property placed in service after Dec. 31, 1980, in taxable years ending after that date, see section 209(a) of Pub. L. 97–34, set out as an Effective Date note under section 168 of this title.

EFFECTIVE DATE; APPLICATION OF FORMER SECTION 453(b) TO CERTAIN DISPOSITIONS

Pub. L. 96–471, § 6(a), Oct. 19, 1980, 94 Stat. 2256, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided:

''(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by sections 2 [enacting this section and sections 453A and 453B of this title and amending sections 311, 336, 337, 381, former section 453, and sections 453B, 481, 644, 691, and 1255 of this title] and 5 [amending section 1239 of this title] shall apply to dispositions made after the date of the enactment of this Act [Oct. 19, 1980] in taxable years ending after such date.

''(2) FOR SECTION 453(e).—Section 453(e) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as amended by section 2) shall apply to first dispositions made after May 14, 1980.

''(3) FOR SECTION 453(h).—Paragraphs (1) and (2) of section 453(h) of such Code (as amended by section 2) shall apply in the case of distributions of installment obligations after March 31, 1980.

''(4) FOR SECTION 453a.—Section 453A of the Internal Revenue Code of 1986 (as amended by section 2) shall apply to taxable years ending after the date of enactment of this Act [Oct. 19, 1980].

''(5) FOR SECTION 453b(f).—Section 453B(f) of the Internal Revenue Code of 1986 (as amended by section 2) shall apply to installment obligations becoming unenforceable after the date of the enactment of this Act [Oct. 19, 1980].

''(6) FOR SECTION 2(c).—The amendments made by section 2(c) [amending sections 336, 337, 453B, and former section 453 of this title] shall take effect as if included in the amendments made by section 403(b) of the Crude Oil Windfall Profit Tax Act of 1980 [see section 403(b)(3) of Pub. L. 96–223, set out as an Effective Date of 1980 Amendments note under section 337 of this title].

''(7) SPECIAL RULE FOR APPLICATION OF FORMER SECTION 453 TO CERTAIN DISPOSITIONS.—In the case of any disposition made on or before the date of the enactment of this Act [Oct. 19, 1980] in any taxable year ending after such date, the provisions of section 453(b) of the Internal Revenue Code of 1986 [see subsec. (b) of former section 453 of this title, set out below] as in effect before such date, shall be applied with respect to such disposition without regard to—

''(A) paragraph (2) of such section 453(b), and

''(B) any requirement that more than 1 payment be received.''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

§ 453A. Special rules for nondealers

(a) General rule

In the case of an installment obligation to which this section applies—

(1) interest shall be paid on the deferred tax liability with respect to such obligation in the manner provided under subsection (c), and

(2) the pledging rules under subsection (d) shall apply.

(b) Installment obligations to which section applies

(1) In general

This section shall apply to any obligation which arises from the disposition of any property under the installment method, but only if the sales price of such property exceeds $150,000.

(2) Special rule for interest payments

For purposes of subsection (a)(1), this section shall apply to an obligation described in paragraph (1) arising during a taxable year only if—

(A) such obligation is outstanding as of the close of such taxable year, and

(B) the face amount of all such obligations held by the taxpayer which arose during, and are outstanding as of the close of, such taxable year exceeds $5,000,000.

Except as provided in regulations, all persons treated as a single employer under subsection (a) or (b) of section 52 shall be treated as one person for purposes of this paragraph and subsection (c)(4).

(3) Exception for personal use and farm property

An installment obligation shall not be treated as described in paragraph (1) if it arises from the disposition—

(A) by an individual of personal use property (within the meaning of section 1275(b)(3)), or

(B) of any property used or produced in the trade or business of farming (within the meaning of section 2032A(e)(4) or (5)).

(4) Special rule for timeshares and residential lots

An installment obligation shall not be treated as described in paragraph (1) if it arises from a disposition described in section 453(*l*)(2)(B), but the provisions of section 453(*l*)(3) (relating to interest payments on

timeshares and residential lots) shall apply to such obligation.

(5) Sales price

For purposes of paragraph (1), all sales or exchanges which are part of the same transaction (or a series of related transactions) shall be treated as 1 sale or exchange.

(c) Interest on deferred tax liability

(1) In general

If an obligation to which this section applies is outstanding as of the close of any taxable year, the tax imposed by this chapter for such taxable year shall be increased by the amount of interest determined in the manner provided under paragraph (2).

(2) Computation of interest

For purposes of paragraph (1), the interest for any taxable year shall be an amount equal to the product of—

(A) the applicable percentage of the deferred tax liability with respect to such obligation, multiplied by

(B) the underpayment rate in effect under section 6621(a)(2) for the month with or within which the taxable year ends.

(3) Deferred tax liability

For purposes of this section, the term ''deferred tax liability'' means, with respect to any taxable year, the product of—

(A) the amount of gain with respect to an obligation which has not been recognized as of the close of such taxable year, multiplied by

(B) the maximum rate of tax in effect under section 1 or 11, whichever is appropriate, for such taxable year.

For purposes of applying the preceding sentence with respect to so much of the gain which, when recognized, will be treated as long-term capital gain, the maximum rate on net capital gain under section 1(h) shall be taken into account.

(4) Applicable percentage

For purposes of this subsection, the term ''applicable percentage'' means, with respect to obligations arising in any taxable year, the percentage determined by dividing—

(A) the portion of the aggregate face amount of such obligations outstanding as of the close of such taxable year in excess of $5,000,000, by

(B) the aggregate face amount of such obligations outstanding as of the close of such taxable year.

(5) Treatment as interest

Any amount payable under this subsection shall be taken into account in computing the amount of any deduction allowable to the taxpayer for interest paid or accrued during the taxable year.

(6) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this subsection including regulations providing for the application of this subsection in the case of contingent payments, short taxable years, and pass-thru entities.

(d) Pledges, etc., of installment obligations

(1) In general

For purposes of section 453, if any indebtedness (hereinafter in this subsection referred to as ''secured indebtedness'') is secured by an installment obligation to which this section applies, the net proceeds of the secured indebtedness shall be treated as a payment received on such installment obligation as of the later of—

(A) the time the indebtedness becomes secured indebtedness, or

(B) the time the proceeds of such indebtedness are received by the taxpayer.

(2) Limitation based on total contract price

The amount treated as received under paragraph (1) by reason of any secured indebtedness shall not exceed the excess (if any) of—

(A) the total contract price, over

(B) any portion of the total contract price received under the contract before the later of the times referred to in subparagraph (A) or (B) of paragraph (1) (including amounts previously treated as received under paragraph (1) but not including amounts not taken into account by reason of paragraph (3)).

(3) Later payments treated as receipt of tax paid amounts

If any amount is treated as received under paragraph (1) with respect to any installment obligation, subsequent payments received on such obligation shall not be taken into account for purposes of section 453 to the extent that the aggregate of such subsequent payments does not exceed the aggregate amount treated as received under paragraph (1).

(4) Secured indebtedness

For purposes of this subsection indebtedness is secured by an installment obligation to the extent that payment of principal or interest on such indebtedness is directly secured (under the terms of the indebtedness or any underlying arrangements) by any interest in such installment obligation. A payment shall be treated as directly secured by an interest in an installment obligation to the extent an arrangement allows the taxpayer to satisfy all or a portion of the indebtedness with the installment obligation.

(e) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section, including regulations—

(1) disallowing the use of the installment method in whole or in part for transactions in which the rules of this section otherwise would be avoided through the use of related persons, pass-thru entities, or intermediaries, and

(2) providing that the sale of an interest in a partnership or other pass-thru entity will be treated as a sale of the proportionate share of the assets of the partnership or other entity.

(Added Pub. L. 96–471, §2(a), Oct. 19, 1980, 94 Stat. 2251; amended Pub. L. 99–514, title VIII, §812(b), Oct. 22, 1986, 100 Stat. 2371; Pub. L. 100–203, title X, §10202(c)[(1)], Dec. 22, 1987, 101 Stat. 1330–390;

Pub. L. 100–647, title I, §1008(g)(2), title II, §2004(d)(2), (7), (8), title V, §5076(a), (b)(1), Nov. 10, 1988, 102 Stat. 3442, 3599, 3600, 3682; Pub. L. 101–239, title VII, §§7812(c)(2), 7815(g), 7821(a)(1)–(3), (4)(B), Dec. 19, 1989, 103 Stat. 2412, 2420, 2423, 2424; Pub. L. 103–66, title XIII, §13201(b)(4), Aug. 10, 1993, 107 Stat. 459; Pub. L. 106–170, title V, §536(b), Dec. 17, 1999, 113 Stat. 1936; Pub. L. 115–97, title I, §13001(b)(2)(C), Dec. 22, 2017, 131 Stat. 2096.)

PRIOR PROVISIONS

Provisions similar to those comprising this section were contained in former section 453 of this title.

AMENDMENTS

2017—Subsec. (c)(3). Pub. L. 115–97 struck out ''or 1201 (whichever is appropriate)'' after ''1(h)'' in concluding provisions.

1999—Subsec. (d)(4). Pub. L. 106–170 inserted at end ''A payment shall be treated as directly secured by an interest in an installment obligation to the extent an arrangement allows the taxpayer to satisfy all or a portion of the indebtedness with the installment obligation.''

1993—Subsec. (c)(3). Pub. L. 103–66 inserted at end ''For purposes of applying the preceding sentence with respect to so much of the gain which, when recognized, will be treated as long-term capital gain, the maximum rate on net capital gain under section 1(h) or 1201 (whichever is appropriate) shall be taken into account.''

1989—Subsec. (b)(2)(B). Pub. L. 101–239, §7821(a)(1), substituted ''such obligations held by the taxpayer'' for ''obligations of the taxpayer described in paragraph (1)''.

Subsec. (b)(3). Pub. L. 101–239, §7815(g), substituted ''Exception for personal use and farm property'' for ''Exception for farm property'' in heading and amended text generally. Prior to amendment, text read as follows: ''An installment obligation shall not be treated as described in paragraph (1) if it arises from the disposition of any property used or produced in the trade or business of farming (within the meaning of section 2032A(e)(4) or (5).''

Pub. L. 101–239, §7812(c)(2), substituted ''(5)).'' for ''(5).''

Subsec. (c)(5), (6). Pub. L. 101–239, §7821(a)(4)(B), added par. (5) and redesignated former par. (5) as (6).

Subsec. (d)(1)(B). Pub. L. 101–239, §7821(a)(3), substituted ''the time the proceeds'' for ''the proceeds''.

Subsec. (d)(2)(B). Pub. L. 101–239, §7821(a)(2), substituted ''the later of the times referred to in subparagraph (A) or (B) of paragraph (1)'' for ''such secured indebtedness was incurred''.

1988—Pub. L. 100–647, §5076(b)(1), struck out ''of real property'' after ''rules for nondealers'' in section catchline.

Subsec. (b)(1). Pub. L. 100–647, §5076(a), amended par. (1) generally. Prior to amendment, par. (1) read as follows: ''This section shall apply to any obligation which arises from the disposition of real property under the installment method which is property used in the taxpayer's trade or business or property held for the production of rental income, but only if the sales price of such property exceeds $150,000.''

Subsec. (b)(2). Pub. L. 100–647, §2004(d)(7), inserted ''and subsection (c)(4)'' after ''of this paragraph'' in last sentence.

Subsec. (b)(3). Pub. L. 100–647, §2004(d)(8), substituted ''farm property'' for ''personal use and farm property'' in heading and amended text generally. Prior to amendment, text read as follows: ''An installment obligation shall not be treated as described in paragraph (1) if it arises from the disposition—

''(A) by an individual of personal use property (within the meaning of section 1275(b)(3)), or

''(B) of any property used or produced in the trade or business of farming (within the meaning of section 2032A(e)(4) or (5)).''

Subsec. (c). Pub. L. 100–647, §1008(g)(2), substituted ''453(k)'' for ''453(j)'' in subsec. (c) as in effect on date before the date of enactment of Pub. L. 100–203 (Dec. 22, 1987).

Subsec. (e). Pub. L. 100–647, §2004(d)(2), added subsec. (e).

1987—Pub. L. 100–203 substituted ''Special rules for nondealers of real property'' for ''Installment method for dealers in personal property'' in section catchline and amended text generally, revising and restating as subsecs. (a) to (d) provisions of former subsecs. (a) to (c).

1986—Subsec. (a)(2). Pub. L. 99–514, §812(b)(1), struck out last sentence which read as follows: ''This paragraph shall not apply with respect to sales of personal property under a revolving credit type plan.''

Subsec. (c). Pub. L. 99–514, §812(b)(2), added subsec. (c).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, see section 13001(c)(1) of Pub. L. 115–97, set out as a note under section 11 of this title.

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106–170 applicable to sales or other dispositions occurring on or after Dec. 17, 1999, see section 536(c) of Pub. L. 106–170, set out as a note under section 453 of this title.

EFFECTIVE DATE OF 1993 AMENDMENT

Amendment by Pub. L. 103–66 applicable to taxable years beginning after Dec. 31, 1992, see section 13201(c) of Pub. L. 103–66, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by sections 7812(c)(2) and 7815(g) of Pub. L. 101–239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 7817 of Pub. L. 101–239, set out as a note under section 1 of this title.

Amendment by section 7821(a)(1)–(3), (4)(B) of Pub. L. 101–239 effective as if included in the provision of the Revenue Act of 1987, Pub. L. 100–203, title X, to which such amendment relates, see section 7823 of Pub. L. 101–239, set out as a note under section 26 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1008(g)(2) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Amendment by section 2004(d)(2), (7), (8) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provisions of the Revenue Act of 1987, Pub. L. 100–203, title X, to which such amendment relates, see section 2004(u) of Pub. L. 100–647, set out as a note under section 56 of this title.

Pub. L. 100–647, title V, §5076(c), Nov. 10, 1988, 102 Stat. 3683, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to sales after December 31, 1988.

''(2) BINDING CONTRACT, ETC.—The amendments made by this section shall not apply to any sale on or before December 31, 1990, if—

''(A) such sale is pursuant to a written binding contract in effect on October 21, 1988, and at all times thereafter before such sale,

''(B) such sale is pursuant to a letter of intent in effect on October 21, 1988, or

''(C) there is a board of directors or shareholder approval for such sale on or before October 21, 1988.''

EFFECTIVE DATE OF 1987 AMENDMENT

Amendment by Pub. L. 100–203 applicable to dispositions in taxable years beginning after Dec. 31, 1987,

with special rules for non-dealers and coordination with Tax Reform Act of 1986, see section 10202(e)(1), (3), (5) of Pub. L. 100–203, set out as a note under section 453 of this title.

EFFECTIVE DATE

For effective date, see section 6(a)(4) of Pub. L. 96–471, set out as a note under section 453 of this title.

CERTAIN REPLEDGES PERMITTED

Pub. L. 100–647, title VI, § 6031, Nov. 10, 1988, 102 Stat. 3695, provided that:

''(a) GENERAL RULE.—Section 453A(d) of the 1986 Code (relating to pledges, etc., of installment obligations) shall not apply to any pledge after December 17, 1987, of an installment obligation to secure any indebtedness if such indebtedness is incurred to refinance indebtedness which was outstanding on December 17, 1987, and which was secured on such date and all times thereafter before such refinancing by a pledge of such installment obligation.

''(b) LIMITATION.—Subsection (a) shall not apply to the extent that the principal amount of the indebtedness resulting from the refinancing exceeds the principal amount of the refinanced indebtedness immediately before the refinancing.

''(c) CERTAIN REFINANCINGS PERMITTED.—For purposes of subsection (a), if—

''(1) a refinancing is attributable to the calling of indebtedness by the creditor, and

''(2) such refinancing is not with the creditor under the refinanced indebtedness or a person related to such creditor,

such refinancing shall, to the extent the refinanced indebtedness qualifies under subsections (a) and (b), be treated as a continuation of such refinanced indebtedness.''

AMENDMENT BY PUB. L. 99–514 TREATED AS CHANGE IN METHOD OF ACCOUNTING

For provisions requiring change in accounting method in the case of any taxpayer who made sales under revolving credit plan and was on installment method under this section for such taxpayer's last taxable year beginning before Jan. 1, 1987, see section 812(c)(2) of Pub. L. 99–514, set out as an Effective Date of 1986 Amendment note under section 453 of this title.

§ 453B. Gain or loss on disposition of installment obligations

(a) General rule

If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and—

(1) the amount realized, in the case of satisfaction at other than face value or a sale or exchange, or

(2) the fair market value of the obligation at the time of distribution, transmission, or disposition, in the case of the distribution, transmission, or disposition otherwise than by sale or exchange.

any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received.

(b) Basis of obligation

The basis of an installment obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

(c) Special rule for transmission at death

Except as provided in section 691 (relating to recipients of income in respect of decedents), this section shall not apply to the transmission of installment obligations at death.

(d) Exception for distributions to which section 337(a) applies

Subsection (a) shall not apply to any distribution to which section 337(a) applies.

(e) Life insurance companies

(1) In general

In the case of a disposition of an installment obligation by any person other than a life insurance company (as defined in section 816(a)) to such an insurance company or to a partnership of which such an insurance company is a partner, no provision of this subtitle providing for the nonrecognition of gain shall apply with respect to any gain resulting under subsection (a). If a corporation which is a life insurance company for the taxable year was (for the preceding taxable year) a corporation which was not a life insurance company, such corporation shall, for purposes of this subsection and subsection (a), be treated as having transferred to a life insurance company, on the last day of the preceding taxable year, all installment obligations which it held on such last day. A partnership of which a life insurance company becomes a partner shall, for purposes of this subsection and subsection (a), be treated as having transferred to a life insurance company, on the last day of the preceding taxable year of such partnership, all installment obligations which it holds at the time such insurance company becomes a partner.

(2) Special rule where life insurance company elects to treat income as not related to insurance business

Paragraph (1) shall not apply to any transfer or deemed transfer of an installment obligation if the life insurance company elects (at such time and in such manner as the Secretary may by regulations prescribe) to determine its life insurance company taxable income—

(A) by returning the income on such installment obligation under the installment method prescribed in section 453, and

(B) as if such income were an item attributable to a noninsurance business.

(3) Noninsurance business

(A) In general

For purposes of this subsection, the term ''noninsurance business'' means any activity which is not an insurance business.

(B) Certain activities treated as insurance businesses

For purposes of subparagraph (A), any activity which is not an insurance business shall be treated as an insurance business if—

(i) it is of a type traditionally carried on by life insurance companies for investment purposes, but only if the carrying on of such activity (other than in the case of real estate) does not constitute the active conduct of a trade or business, or

(ii) it involves the performance of administrative services in connection with plans providing life insurance, pension, or accident and health benefits.

(f) Obligation becomes unenforceable

For purposes of this section, if any installment obligation is canceled or otherwise becomes unenforceable—

(1) the obligation shall be treated as if it were disposed of in a transaction other than a sale or exchange, and

(2) if the obligor and obligee are related persons (within the meaning of section 453(f)(1)), the fair market value of the obligation shall be treated as not less than its face amount.

(g) Transfers between spouses or incident to divorce

In the case of any transfer described in subsection (a) of section 1041 (other than a transfer in trust)—

(1) subsection (a) of this section shall not apply, and

(2) the same tax treatment with respect to the transferred installment obligation shall apply to the transferee as would have applied to the transferor.

(h) Certain liquidating distributions by S corporations

If—

(1) an installment obligation is distributed by an S corporation in a complete liquidation, and

(2) receipt of the obligation is not treated as payment for the stock by reason of section 453(h)(1),

then, except for purposes of any tax imposed by subchapter S, no gain or loss with respect to the distribution of the obligation shall be recognized by the distributing corporation. Under regulations prescribed by the Secretary, the character of the gain or loss to the shareholder shall be determined in accordance with the principles of section 1366(b).

(Added Pub. L. 96–471, § 2(a), Oct. 19, 1980, 94 Stat. 2252; amended Pub. L. 96–471, § 2(c)(3), Oct. 19, 1980, 94 Stat. 2254; Pub. L. 97–448, title III, § 302, Jan. 12, 1983, 96 Stat. 2398; Pub. L. 98–369, div. A, title I, § 43(c)(2), title II, § 211(b)(6), title IV, §§ 421(b)(3), 492(b)(3), July 18, 1984, 98 Stat. 558, 754, 794, 854; Pub. L. 99–514, title VI, § 631(e)(9), title X, § 1011(b)(1), title XVIII, § 1842(c), Oct. 22, 1986, 100 Stat. 2274, 2389, 2853; Pub. L. 100–647, title I, § 1006(e)(22), Nov. 10, 1988, 102 Stat. 3403; Pub. L. 101–508, title XI, § 11702(a)(2), Nov. 5, 1990, 104 Stat. 1388–514; Pub. L. 115–97, title I, § 13512(b)(1), Dec. 22, 2017, 131 Stat. 2142; Pub. L. 115–141, div. U, title IV, § 401(a)(111), Mar. 23, 2018, 132 Stat. 1189.)

PRIOR PROVISIONS

Provisions similar to those comprising this section were contained in former section 453 of this title.

AMENDMENTS

2018—Pub. L. 115–141 substituted ''loss on disposition'' for ''loss disposition'' in section catchline.

2017—Subsec. (e)(2)(B). Pub. L. 115–97, § 13512(b)(1)(A), struck out ''(as defined in section 806(b)(3))'' before period at end.

Subsec. (e)(3). Pub. L. 115–97, § 13512(b)(1)(B), added par. (3).

1990—Subsec. (d). Pub. L. 101–508 substituted heading for one which read: ''Effect of distribution in liquidations to which section 332 applies'' and amended text generally. Prior to amendment, text read as follows: ''If—

''(1) an installment obligation is distributed in a liquidation to which section 332 (relating to complete liquidations of subsidiaries) applies, and

''(2) the basis of such obligation in the hands of the distributee is determined under section 334(b)(1),

then no gain or loss with respect to the distribution of such obligation shall be recognized by the distributing corporation.''

1988—Subsec. (h). Pub. L. 100–647 added subsec. (h).

1986—Subsec. (d). Pub. L. 99–514, § 631(e)(9), amended subsec. (d) generally, substituting ''liquidations to which section 332 applies'' for ''certain liquidations'' in heading, striking out par. (1) designation, redesignating subpars. (A) and (B) as pars. (1) and (2), and striking out former par. (2) relating to liquidations to which section 337 applies.

Subsec. (e)(2)(B). Pub. L. 99–514, § 1011(b)(1), substituted ''section 806(b)(3)'' for ''section 806(c)(3)''.

Subsec. (g). Pub. L. 99–514, § 1842(c), inserted ''(other than a transfer in trust)''.

1984—Subsec. (d)(2). Pub. L. 98–369, § 492(b)(3), struck out ''1251(c),'' after ''1250(a),'' in provision following subpar. (B).

Pub. L. 98–369, § 43(c)(2), substituted ''1254(a), or 1276(a)'' for ''or 1254(a)''.

Subsec. (e)(1). Pub. L. 98–369, § 211(b)(6)(A), substituted ''section 816(a)'' for ''section 801(a)''.

Subsec. (e)(2). Pub. L. 98–369, § 211(b)(6)(B), substituted ''as not related to insurance business'' for ''as investment income'' in heading, and in text substituted ''as if such income were an item attributable to a noninsurance business (as defined in section 806(c)(3))'' for ''if such income would not otherwise be returnable as an item referred to in section 804(b) or as long-term capital gain, as if the income on such obligations were income specified in section 804(b)''.

Subsec. (g). Pub. L. 98–369, § 421(b)(3), added subsec. (g).

1983—Subsec. (d)(2). Pub. L. 97–448 substituted ''under subsection (a)'' for ''under paragraph (1)'' in second sentence.

1980—Subsec. (d). Pub. L. 96–471, § 2(c)(3), inserted last sentence providing that in the case of any installment obligation which would have met the requirements of subpars. (A) and (B) of par. (2) but for sections 337(f), gain shall be recognized to such corporation by reason of such distribution only to the extent gain would have been recognized under sections 337(f) if such corporation had sold or exchanged such installment obligation on the date of such distribution.

EFFECTIVE DATE OF 2017 AMENDMENT

Pub. L. 115–97, title I, § 13512(c), Dec. 22, 2017, 131 Stat. 2143, provided that: ''The amendments made by this section [amending this section and sections 465, 801, 804, 805, 842, and 953 of this title and repealing section 806 of this title] shall apply to taxable years beginning after December 31, 2017.''

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101–508 effective as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 11702(j) of Pub. L. 101–508, set out as a note under section 59 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 631(e)(9) of Pub. L. 99–514 applicable to any distribution in complete liquidation, and any sale or exchange, made by a corporation after July 31, 1986, unless such corporation is completely liquidated before Jan. 1, 1987, any transaction described in section 338 of this title for which the acquisition date occurs after Dec. 31, 1986, and any distribution, not in complete liquidation, made after Dec. 31, 1986, with exceptions and special and transitional rules, see section 633 of Pub. L. 99–514, set out as an Effective Date note under section 336 of this title.

Pub. L. 99–514, title X, §1011(c)(1), Oct. 22, 1986, 100 Stat. 2389, provided that: ''The amendments made by this section [amending this section and sections 465, 801, 804 to 806, 813, and 815 of this title, enacting provisions set out as a note under section 801 of this title, and amending provisions set out as a note under section 806 of this title] shall apply to taxable years beginning after December 31, 1986.''

Amendment by section 1842(c) of Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 43(c)(2) of Pub. L. 98–369 applicable to taxable years ending after July 18, 1984, see section 44 of Pub. L. 98–369, set out as an Effective Date note under section 1271 of this title.

Amendment by section 211(b)(6) of Pub. L. 98–369 applicable to taxable years beginning after Dec. 31, 1983, see section 215 of Pub. L. 98–369, set out as an Effective Date note under section 801 of this title.

Amendment by section 421(b)(3) of Pub. L. 98–369 applicable to transfers after July 18, 1984, in taxable years ending after such date, subject to election to have amendment apply to transfers after 1983 or to transfers pursuant to existing decrees, see section 421(d) of Pub. L. 98–369, set out as an Effective Date note under section 1041 of this title.

Amendment by section 492(b)(3) of Pub. L. 98–369 applicable to taxable years beginning after Dec. 31, 1983, see section 492(d) of Pub. L. 98–369, set out as a note under section 170 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97–448 applicable to dispositions made after Oct. 19, 1980, in taxable years ending after such date, see section 311(a) of Pub. L. 97–448, set out as a note under section 453 of this title.

EFFECTIVE DATE OF 1980 AMENDMENT

For effective date of amendment by Pub. L. 96–471, see section 6(a)(6) of Pub. L. 96–471, set out as an Effective Date note under section 453 of this title.

EFFECTIVE DATE

For effective date, see section 6(a)(1), (5) of Pub. L. 96–471, set out as a note under section 453 of this title.

REPEAL OF MODIFICATION OF INSTALLMENT METHOD

Pub. L. 106–573, §2, Dec. 28, 2000, 114 Stat. 3061, provided that:

''(a) IN GENERAL.—Subsection (a) of section 536 of the Ticket to Work and Work Incentives Improvement Act of 1999 (relating to modification of installment method and repeal of installment method for accrual method taxpayers) [Pub. L. 106–170, amending this section] is repealed effective with respect to sales and other dispositions occurring on or after the date of the enactment of such Act [Dec. 17, 1999].

''(b) APPLICABILITY.—The Internal Revenue Code of 1986 shall be applied and administered as if that subsection (and the amendments made by that subsection) had not been enacted.''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101–1147 and 1171–1177] or title XVIII [§§1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

TREATMENT OF ELECTIONS UNDER SECTION 453B(e)(2)

Pub. L. 98–369, div. A, title II, §217(b), July 18, 1984, 98 Stat. 762, as amended by Pub. L. 99–514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: ''If an election is made under section 453B(e)(2) before January 1, 1984, with respect to any installment obligation, any income from such obligation shall be treated as attributable to a noninsurance business (as defined in [former] section 806(c)(3) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]).''

[§ 453C. Repealed. Pub. L. 100–203, title X, § 10202(a)(1), Dec. 22, 1987, 101 Stat. 1330–388]

Section, added Pub. L. 99–514, title VIII, §811(a), Oct. 22, 1986, 100 Stat. 2365; amended Pub. L. 100–647, title I, §1008(f)(1)–(5), Nov. 10, 1988, 102 Stat. 3441, 3442, related to treatment of certain indebtedness as payment on installment obligations.

EFFECTIVE DATE OF REPEAL

Repeal applicable to dispositions in taxable years beginning after Dec. 31, 1987, with special rules for dealers and non-dealers, and coordination with Tax Reform Act of 1986, see section 10202(e)(1)–(3), (5) of Pub. L. 100–203, set out as a note under section 453 of this title.

APPLICABILITY OF AMENDMENTS BY PUB. L. 100–203 AND PUB. L. 100–647

Pub. L. 100–647, title I, §1008(f)(9), Nov. 10, 1988, 102 Stat. 3442, provided that: ''For purposes of applying the amendments made by this subsection [amending this section and provisions set out below] and the amendments made by section 10202 of the Revenue Act of 1987 [Pub. L. 100–203, amending sections 56, 381, 453, 453A, and 691 of this title and repealing this section], the provisions of this subsection shall be treated as having been enacted immediately before the enactment of the Revenue Act of 1987 [Dec. 22, 1987].''

EFFECTIVE DATE; ALLOCATION OF INDEBTEDNESS AS PAYMENT ON INSTALLMENT OBLIGATION

Pub. L. 99–514, title VIII, §811(c), Oct. 22, 1986, 100 Stat. 2368, as amended by Pub. L. 100–647, title I, §1008(f)(6)–(8), Nov. 10, 1988, 102 Stat. 3442; Pub. L. 105–34, title X, §1088(a), Aug. 5, 1997, 111 Stat. 959, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this section, the amendments made by this section [enacting this section] shall apply to taxable years ending after December 31, 1986, with respect to dispositions after February 28, 1986.

''[(2) Repealed. Pub. L. 105–34, title X, §1088(a), Aug. 5, 1997, 111 Stat. 959.]

''(3) EXCEPTION FOR CERTAIN OBLIGATIONS.—In applying the amendments made by this section to any installment obligation of a corporation incorporated on January 13, 1928, the following indebtedness shall not be taken into account in determining the allocable installment indebtedness of such corporation under section 453C of the Internal Revenue Code of 1986 (as added by this section):

''(A) 12⅝ percent subordinated debentures with a total face amount of $175,000,000 issued pursuant to a trust indenture dated as of September 1, 1985.

''(B) A revolving credit term loan in the maximum amount of $130,000,000 made pursuant to a revolving

credit and security agreement dated as of September 6, 1985, payable in various stages with final payment due on August 31, 1992.

This paragraph shall also apply to indebtedness which replaces indebtedness described in this paragraph if such indebtedness does not exceed the amount and maturity of the indebtedness it replaces.

''(4) SPECIAL RULE FOR RESIDENTIAL CONDOMINIUM PROJECT.—For purposes of applying the amendments made by this section, the term applicable installment obligation (within the meaning of section 453C(e)(1) of the Internal Revenue Code of 1986) shall not include any obligation arising in connection with sales from a residential condominium project—

''(A) for which a contract to purchase land for the project was entered into at least 5 years before the date of the enactment of this Act,

''(B) with respect to which land for the project was purchased before September 26, 1985,

''(C) with respect to which building permits for the project were obtained, and construction commenced, before September 26, 1985,

''(D) in conjunction with which not less than 80 units of low-income housing are deeded to a tax-exempt organization designated by a local government, and

''(E) with respect to which at least $1,000,000 of expenses were incurred before September 26, 1985.

''(5) SPECIAL RULE FOR QUALIFIED BUYOUT.—The amendments made by this section shall apply for taxable years ending after December 31, 1991, to a corporation if—

''(A) such corporation was incorporated on May 25, 1984, for the purpose of acquiring all of the stock of another corporation,

''(B) such acquisition took place on October 23, 1984,

''(C) in connection with such acquisition, the corporation incurred indebtedness of approximately $151,000,000, and

''(D) substantially all of the stock of the corporation is owned directly or indirectly by employees of the corporation the stock of which was acquired on October 23, 1984.

''(6) SPECIAL RULE FOR SALES OF REAL PROPERTY BY DEALERS.—In the case of installment obligations arising from the sale of real property in the ordinary course of the trade or business of the taxpayer, any gain attributable to allocable installment indebtedness allocated to any such installment obligations which arise (or are deemed to arise)—

''(A) in the 1st taxable year of the taxpayer ending after December 31, 1986, shall be taken into account ratably over the 3 taxable years beginning with such 1st taxable year, and

''(B) in the 2nd taxable year of the taxpayer ending after December 31, 1986, shall be taken into account ratably over the 2 taxable years beginning with such 2nd taxable year.

''(7) SPECIAL RULE FOR SALES OF PERSONAL PROPERTY BY DEALERS.—In the case of installment obligations arising from the sale of personal property in the ordinary course of the trade or business of the taxpayer, solely for purposes of determining the time for payment of tax and interest payable with respect to such tax—

''(A) any increase in tax imposed by chapter 1 of the Internal Revenue Code of 1986 for the 1st taxable year of the taxpayer ending after December 31, 1986, by reason of the amendments made by this section shall be treated as imposed ratably over the 3 taxable years beginning with such 1st taxable year, and

''(B) any increase in tax imposed by such chapter 1 for the 2nd taxable year of the taxpayer ending after December 31, 1986 (determined without regard to subparagraph (A)), by reason of the amendments made by this section shall be treated as imposed ratably over the 2 taxable years beginning with such 2nd taxable year.

''(8) TREATMENT OF CERTAIN INSTALLMENT OBLIGATIONS.—Notwithstanding the amendments made by subtitle B of title III [section 311 of Pub. L. 99–514, amending sections 593, 631, 852, 1201, and 1445 of this title and enacting provisions set out as notes under sections 631 and 1201 of this title], gain with respect to installment payments received pursuant to notes issued in accordance with a note agreement dated as of August 29, 1980, where—

''(A) such note agreement was executed pursuant to an agreement of purchase and sale dated April 25, 1980,

''(B) more than ½ of the installment payments of the aggregate principal of such notes have been received by August 29, 1986, and

''(C) the last installment payment of the principal of such notes is due August 29, 1989,

shall be taxed at a rate of 28 percent.

''(9) SPECIAL RULES.—For purposes of section 453C of the 1986 Code (as added by subsection (a))—

''(A) REVOLVING CREDIT PLANS, ETC.—The term 'applicable installment obligation' shall not include any obligation arising out of any disposition or sale described in paragraph (1) or (2) of section 453(k) of such Code (as added by section 812(a)).

''(B) CERTAIN DISPOSITIONS DEEMED MADE ON FIRST DAY OF TAXABLE YEAR.—In the case of a taxpayer's 1st taxable year ending after December 31, 1986, dispositions after February 28, 1986, and before the 1st day of such taxable year shall be treated as made on such 1st day.''

[Pub. L. 105–34, title X, § 1088(b), Aug. 5, 1997, 111 Stat. 959, as amended by Pub. L. 105–206, title VI, § 6010(q), July 22, 1998, 112 Stat. 817, provided that:

[''(1) IN GENERAL.—The amendment made by this section [amending section 811(c) of Pub. L. 99–514, set out above] shall apply to taxable years beginning more than 1 year after the date of the enactment of this Act [Aug. 5, 1997].

[''(2) COORDINATION WITH SECTION 481.—In the case of any taxpayer required by this section to change its method of accounting for any taxable year—

[''(A) such changes shall be treated as initiated by the taxpayer,

[''(B) such changes shall be treated as made with the consent of the Secretary of the Treasury, and

[''(C) the net amount of the adjustments required to be taken into account under section 481(a) of the Internal Revenue Code of 1986 shall be taken into account ratably over the 4 taxable year period beginning with the first taxable year beginning more than 1 year after the date of the enactment of this Act.'']

§ 454. Obligations issued at discount

(a) Non-interest-bearing obligations issued at a discount

If, in the case of a taxpayer owning any non-interest-bearing obligation issued at a discount and redeemable for fixed amounts increasing at stated intervals or owning an obligation described in paragraph (2) of subsection (c), the increase in the redemption price of such obligation occurring in the taxable year does not (under the method of accounting used in computing his taxable income) constitute income to him in such year, such taxpayer may, at his election made in his return for any taxable year, treat such increase as income received in such taxable year. If any such election is made with respect to any such obligation, it shall apply also to all such obligations owned by the taxpayer at the beginning of the first taxable year to which it applies and to all such obligations thereafter acquired by him and shall be binding for all subsequent taxable years, unless on application by the taxpayer the Secretary permits him, subject to such conditions as the Secretary deems necessary, to change to a different meth-

od. In the case of any such obligations owned by the taxpayer at the beginning of the first taxable year to which his election applies, the increase in the redemption price of such obligations occurring between the date of acquisition (or, in the case of an obligation described in paragraph (2) of subsection (c), the date of acquisition of the series E bond involved) and the first day of such taxable year shall also be treated as income received in such taxable year.

(b) Short-term obligations issued on discount basis

In the case of any obligation—

(1) of the United States; or

(2) of a State or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia,

which is issued on a discount basis and payable without interest at a fixed maturity date not exceeding 1 year from the date of issue, the amount of discount at which such obligation is originally sold shall not be considered to accrue until the date on which such obligation is paid at maturity, sold, or otherwise disposed of.

(c) Matured United States savings bonds

In the case of a taxpayer who—

(1) holds a series E United States savings bond at the date of maturity, and

(2) pursuant to regulations prescribed under chapter 31 of title 31 (A) retains his investment in such series E bond in an obligation of the United States, other than a current income obligation, or (B) exchanges such series E bond for another nontransferable obligation of the United States in an exchange upon which gain or loss is not recognized because of section 1037 (or so much of section 1031 as relates to section 1037),

the increase in redemption value (to the extent not previously includible in gross income) in excess of the amount paid for such series E bond shall be includible in gross income in the taxable year in which the obligation is finally redeemed or in the taxable year of final maturity, whichever is earlier. This subsection shall not apply to a corporation, and shall not apply in the case of any taxable year for which the taxpayer's taxable income is computed under an accrual method of accounting or for which an election made by the taxpayer under subsection (a) applies.

(Aug. 16, 1954, ch. 736, 68A Stat. 156; Pub. L. 86–346, title I, §102, Sept. 22, 1959, 73 Stat. 621; Pub. L. 94–455, title XIX, §§1901(c)(2), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1803, 1834; Pub. L. 97–452, §2(c)(2), Jan. 12, 1983, 96 Stat. 2478.)

AMENDMENTS

1983—Subsec. (c)(2). Pub. L. 97–452 substituted ''chapter 31 of title 31'' for ''the Second Liberty Bond Act''.

1976—Subsec. (a). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary'' in two places.

Subsec. (b)(2). Pub. L. 94–455, §1901(c)(2), struck out '', a Territory,'' after ''a State''.

1959—Subsec. (c)(2). Pub. L. 86–346 designated existing provisions as cl. (A), inserted ''of the United States'' after ''an obligation'' and struck out ''the maturity value of'' before ''such series E bond'' and ''which matures not more than 10 years from the date of maturity of such series E bond'' after ''income obligation'' in such cl. (A), and added cl. (B).

§ 455. Prepaid subscription income

(a) Year in which included

Prepaid subscription income to which this section applies shall be included in gross income for the taxable years during which the liability described in subsection (d)(2) exists.

(b) Where taxpayer's liability ceases

In the case of any prepaid subscription income to which this section applies—

(1) If the liability described in subsection (d)(2) ends, then so much of such income as was not includible in gross income under subsection (a) for preceding taxable years shall be included in gross income for the taxable year in which the liability ends.

(2) If the taxpayer dies or ceases to exist, then so much of such income as was not includible in gross income under subsection (a) for preceding taxable years shall be included in gross income for the taxable year in which such death, or such cessation of existence, occurs.

(c) Prepaid subscription income to which this section applies

(1) Election of benefits

This section shall apply to prepaid subscription income if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such income is received. The election shall be made in such manner as the Secretary may by regulations prescribe. No election may be made with respect to a trade or business if in computing taxable income the cash receipts and disbursements method of accounting is used with respect to such trade or business.

(2) Scope of election

An election made under this section shall apply to all prepaid subscription income received in connection with the trade or business with respect to which the taxpayer has made the election; except that the taxpayer may, to the extent permitted under regulations prescribed by the Secretary, include in gross income for the taxable year of receipt the entire amount of any prepaid subscription income if the liability from which it arose is to end within 12 months after the date of receipt. An election made under this section shall not apply to any prepaid subscription income received before the first taxable year for which the election is made.

(3) When election may be made

(A) With consent

A taxpayer may, with the consent of the Secretary, make an election under this section at any time.

(B) Without consent

A taxpayer may, without the consent of the Secretary, make an election under this section for his first taxable year in which he receives prepaid subscription income in the trade or business. Such election shall be made not later than the time prescribed by

law for filing the return for the taxable year (including extensions thereof) with respect to which such election is made.

(4) Period to which election applies

An election under this section shall be effective for the taxable year with respect to which it is first made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election. For purposes of this title, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

(d) Definitions

For purposes of this section—

(1) Prepaid subscription income

The term ''prepaid subscription income'' means any amount (includible in gross income) which is received in connection with, and is directly attributable to, a liability which extends beyond the close of the taxable year in which such amount is received, and which is income from a subscription to a newspaper, magazine, or other periodical.

(2) Liability

The term ''liability'' means a liability to furnish or deliver a newspaper, magazine, or other periodical.

(3) Receipt of prepaid subscription income

Prepaid subscription income shall be treated as received during the taxable year for which it is includible in gross income under section 451 (without regard to this section).

(e) Deferral of income under established accounting procedures

Notwithstanding the provisions of this section, any taxpayer who has, for taxable years prior to the first taxable year to which this section applies, reported his income under an established and consistent method or practice of accounting for prepaid subscription income (to which this section would apply if an election were made) may continue to report his income for taxable years to which this title applies in accordance with such method or practice.

(Added Pub. L. 85–866, title I, § 28(a), Sept. 2, 1958, 72 Stat. 1625; amended Pub. L. 94–455, title XIX, §§ 1901(a)(67), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1775, 1834.)

AMENDMENTS

1976—Subsec. (c). Pub. L. 94–455, § 1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary'' wherever appearing.

Subsec. (c)(3)(B). Pub. L. 94–455, § 1901(a)(67), substituted ''for his first taxable year in which he receives prepaid subscription income in the trade or business'' for ''for his first taxable year (i) which begins after December 31, 1957, and (ii) in which he receives prepaid subscription income in the trade or business''.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(67) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

EFFECTIVE DATE

Pub. L. 85–866, title I, § 28(c), Sept. 2, 1958, 72 Stat. 1626, provided that: ''The amendments made by subsections (a) and (b) [enacting this section] shall apply with respect to taxable years beginning after December 31, 1957.''

§ 456. Prepaid dues income of certain membership organizations

(a) Year in which included

Prepaid dues income to which this section applies shall be included in gross income for the taxable years during which the liability described in subsection (e)(2) exists.

(b) Where taxpayer's liability ceases

In the case of any prepaid dues income to which this section applies—

(1) If the liability described in subsection (e)(2) ends, then so much of such income as was not includible in gross income under subsection (a) for preceding taxable years shall be included in gross income for the taxable year in which the liability ends.

(2) If the taxpayer ceases to exist, then so much of such income as was not includible in gross income under subsection (a) for preceding taxable years shall be included in gross income for the taxable year in which such cessation of existence occurs.

(c) Prepaid dues income to which this section applies

(1) Election of benefits

This section shall apply to prepaid dues income if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such income is received. The election shall be made in such manner as the Secretary may by regulations prescribe. No election may be made with respect to a trade or business if in computing taxable income the cash receipts and disbursements method of accounting is used with respect to such trade or business.

(2) Scope of election

An election made under this section shall apply to all prepaid dues income received in connection with the trade or business with respect to which the taxpayer has made the election; except that the taxpayer may, to the extent permitted under regulations prescribed by the Secretary, include in gross income for the taxable year of receipt the entire amount of any prepaid dues income if the liability from which it arose is to end within 12 months after the date of receipt. Except as provided in subsection (d), and election made under this section shall not apply to any prepaid dues income received before the first taxable year for which the election is made.

(3) When election may be made

(A) With consent

A taxpayer may, with the consent of the Secretary, make an election under this section at any time.

(B) Without consent

A taxpayer may, without the consent of the Secretary, make an election under this section for its first taxable year in which it receives prepaid dues income in the trade or business. Such election shall be made not

later than the time prescribed by law for filing the return for the taxable year (including extensions thereof) with respect to which such election is made.

(4) Period to which election applies

An election under this section shall be effective for the taxable year with respect to which it is first made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election. For purposes of this title, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

(d) Transitional rule

(1) Amount includible in gross income for election years

If a taxpayer makes an election under this section with respect to prepaid dues income, such taxpayer shall include in gross income, for each taxable year to which such election applies, not only that portion of prepaid dues income received in such year otherwise includible in gross income for such year under this section, but shall also include in gross income for such year an additional amount equal to the amount of prepaid dues income received in the 3 taxable years preceding the first taxable year to which such election applies which would have been included in gross income in the taxable year had the election been effective 3 years earlier.

(2) Deductions of amounts included in income more than once

A taxpayer who makes an election with respect to prepaid dues income, and who includes in gross income for any taxable year to which the election applies an additional amount computed under paragraph (1), shall be permitted to deduct, for such taxable year and for each of the 4 succeeding taxable years, an amount equal to one-fifth of such additional amount, but only to the extent that such additional amount was also included in the taxpayer's gross income during any of the 3 taxable years preceding the first taxable year to which such election applies.

(e) Definitions

For purposes of this section—

(1) Prepaid dues income

The term ''prepaid dues income'' means any amount (includible in gross income) which is received by a membership organization in connection with, and is directly attributable to, a liability to render services or make available membership privileges over a period of time which extends beyond the close of the taxable year in which such amount is received.

(2) Liability

The term ''liability'' means a liability to render services or make available membership privileges over a period of time which does not exceed 36 months, which liability shall be deemed to exist ratably over the period of time that such services are required to be rendered, or that such membership privileges are required to be made available.

(3) Membership organization

The term ''membership organization'' means a corporation, association, federation, or other organization—

(A) organized without capital stock of any kind, and

(B) no part of the net earnings of which is distributable to any member.

(4) Receipt of prepaid dues income

Prepaid dues income shall be treated as received during the taxable year for which it is includible in gross income under section 451 (without regard to this section).

(Added Pub. L. 87–109, §1(a), July 26, 1961, 75 Stat. 222; amended Pub. L. 94–455, title XIX, §§1901(a)(68), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1775, 1834.)

AMENDMENTS

1976—Subsec. (c). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary'' wherever appearing.

Subsec. (c)(3)(B). Pub. L. 94–455, §1901(a)(68), substituted ''for its first taxable year'' for ''for its first taxable year (i) which begins after December 31, 1960, and (ii)''.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(68) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

EFFECTIVE DATE

Pub. L. 87–109, §2, July 26, 1961, 75 Stat. 224, provided that: ''The amendments made by this Act [enacting this section] shall apply with respect to taxable years beginning after December 31, 1960.''

§ 457. Deferred compensation plans of State and local governments and tax-exempt organizations

(a) Year of inclusion in gross income

(1) In general

Any amount of compensation deferred under an eligible deferred compensation plan, and any income attributable to the amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income—

(A) is paid to the participant or other beneficiary, in the case of a plan of an eligible employer described in subsection (e)(1)(A), and

(B) is paid or otherwise made available to the participant or other beneficiary, in the case of a plan of an eligible employer described in subsection (e)(1)(B).

(2) Special rule for rollover amounts

To the extent provided in section 72(t)(9), section 72(t) shall apply to any amount includible in gross income under this subsection.

(3) Special rule for health and long-term care insurance

In the case of a plan of an eligible employer described in subsection (e)(1)(A), to the extent provided in section 402(*l*), paragraph (1) shall not apply to amounts otherwise includible in gross income under this subsection.

(b) Eligible deferred compensation plan defined

For purposes of this section, the term ''eligible deferred compensation plan'' means a plan established and maintained by an eligible employer—

(1) in which only individuals who perform service for the employer may be participants,

(2) which provides that (except as provided in paragraph (3)) the maximum amount which may be deferred under the plan for the taxable year (other than rollover amounts) shall not exceed the lesser of—

(A) the applicable dollar amount, or

(B) 100 percent of the participant's includible compensation,

(3) which may provide that, for 1 or more of the participant's last 3 taxable years ending before he attains normal retirement age under the plan, the ceiling set forth in paragraph (2) shall be the lesser of—

(A) twice the dollar amount in effect under subsection (b)(2)(A), or

(B) the sum of—

(i) the plan ceiling established for purposes of paragraph (2) for the taxable year (determined without regard to this paragraph), plus

(ii) so much of the plan ceiling established for purposes of paragraph (2) for taxable years before the taxable year as has not previously been used under paragraph (2) or this paragraph,

(4) which provides that compensation will be deferred for any calendar month only if an agreement providing for such deferral has been entered into before the beginning of such month,

(5) which meets the distribution requirements of subsection (d), and

(6) except as provided in subsection (g), which provides that—

(A) all amounts of compensation deferred under the plan,

(B) all property and rights purchased with such amounts, and

(C) all income attributable to such amounts, property, or rights,

shall remain (until made available to the participant or other beneficiary) solely the property and rights of the employer (without being restricted to the provision of benefits under the plan), subject only to the claims of the employer's general creditors.

A plan which is established and maintained by an employer which is described in subsection (e)(1)(A) and which is administered in a manner which is inconsistent with the requirements of any of the preceding paragraphs shall be treated as not meeting the requirements of such paragraph as of the 1st plan year beginning more than 180 days after the date of notification by the Secretary of the inconsistency unless the employer corrects the inconsistency before the 1st day of such plan year.

(c) Limitation

The maximum amount of the compensation of any one individual which may be deferred under subsection (a) during any taxable year shall not exceed the amount in effect under subsection (b)(2)(A) (as modified by any adjustment provided under subsection (b)(3)).

(d) Distribution requirements

(1) In general

For purposes of subsection (b)(5), a plan meets the distribution requirements of this subsection if—

(A) under the plan amounts will not be made available to participants or beneficiaries earlier than—

(i) the calendar year in which the participant attains age 70½ (in the case of a plan maintained by an employer described in subsection (e)(1)(A), age 59½),

(ii) when the participant has a severance from employment with the employer,

(iii) when the participant is faced with an unforeseeable emergency (determined in the manner prescribed by the Secretary in regulations), or

(iv) except as may be otherwise provided by regulations, in the case of a plan maintained by an employer described in subsection (e)(1)(A), with respect to amounts invested in a lifetime income investment (as defined in section 401(a)(38)(B)(ii)), the date that is 90 days prior to the date that such lifetime income investment may no longer be held as an investment option under the plan,

(B) the plan meets the minimum distribution requirements of paragraph (2),

(C) in the case of a plan maintained by an employer described in subsection (e)(1)(A), the plan meets requirements similar to the requirements of section 401(a)(31), and

(D) except as may be otherwise provided by regulations, in the case of amounts described in subparagraph (A)(iv), such amounts will be distributed only in the form of a qualified distribution (as defined in section 401(a)(38)(B)(i)) or a qualified plan distribution annuity contract (as defined in section 401(a)(38)(B)(iv)).

Any amount transferred in a direct trustee-to-trustee transfer in accordance with section 401(a)(31) shall not be includible in gross income for the taxable year of transfer.

(2) Minimum distribution requirements

A plan meets the minimum distribution requirements of this paragraph if such plan meets the requirements of section 401(a)(9).

(3) Special rule for government plan

An eligible deferred compensation plan of an employer described in subsection (e)(1)(A) shall not be treated as failing to meet the requirements of this subsection solely by reason of making a distribution described in subsection (e)(9)(A).

(e) Other definitions and special rules

For purposes of this section—

(1) Eligible employer

The term ''eligible employer'' means—

(A) a State, political subdivision of a State, and any agency or instrumentality of

a State or political subdivision of a State, and

(B) any other organization (other than a governmental unit) exempt from tax under this subtitle.

(2) Performance of service

The performance of service includes performance of service as an independent contractor and the person (or governmental unit) for whom such services are performed shall be treated as the employer.

(3) Participant

The term ''participant'' means an individual who is eligible to defer compensation under the plan.

(4) Beneficiary

The term ''beneficiary'' means a beneficiary of the participant, his estate, or any other person whose interest in the plan is derived from the participant.

(5) Includible compensation

The term ''includible compensation'' has the meaning given to the term ''participant's compensation'' by section 415(c)(3).

(6) Compensation taken into account at present value

Compensation shall be taken into account at its present value.

(7) Community property laws

The amount of includible compensation shall be determined without regard to any community property laws.

(8) Income attributable

Gains from the disposition of property shall be treated as income attributable to such property.

(9) Benefits of tax exempt organization plans not treated as made available by reason of certain elections, etc.

In the case of an eligible deferred compensation plan of an employer described in subsection (e)(1)(B)—

(A) Total amount payable is dollar limit or less

The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if—

(i) the portion of such amount which is not attributable to rollover contributions (as defined in section 411(a)(11)(D)) does not exceed the dollar limit under section 411(a)(11)(A), and

(ii) such amount may be distributed only if—

(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and

(II) there has been no prior distribution under the plan to such participant to which this subparagraph applied.

A plan shall not be treated as failing to meet the distribution requirements of subsection (d) by reason of a distribution to which this subparagraph applies.

(B) Election to defer commencement of distributions

The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to defer commencement of distributions under the plan if—

(i) such election is made after amounts may be available under the plan in accordance with subsection (d)(1)(A) and before commencement of such distributions, and

(ii) the participant may make only 1 such election.

(10) Transfers between plans

A participant shall not be required to include in gross income any portion of the entire amount payable to such participant solely by reason of the transfer of such portion from 1 eligible deferred compensation plan to another eligible deferred compensation plan.

(11) Certain plans excluded

(A) In general

The following plans shall be treated as not providing for the deferral of compensation:

(i) Any bona fide vacation leave, sick leave, compensatory time, severance pay, disability pay, or death benefit plan.

(ii) Any plan paying solely length of service awards to bona fide volunteers (or their beneficiaries) on account of qualified services performed by such volunteers.

(B) Special rules applicable to length of service award plans

(i) Bona fide volunteer

An individual shall be treated as a bona fide volunteer for purposes of subparagraph (A)(ii) if the only compensation received by such individual for performing qualified services is in the form of—

(I) reimbursement for (or a reasonable allowance for) reasonable expenses incurred in the performance of such services, or

(II) reasonable benefits (including length of service awards), and nominal fees for such services, customarily paid by eligible employers in connection with the performance of such services by volunteers.

(ii) Limitation on accruals

A plan shall not be treated as described in subparagraph (A)(ii) if the aggregate amount of length of service awards accruing with respect to any year of service for any bona fide volunteer exceeds $6,000.

(iii) Cost of living adjustment

In the case of taxable years beginning after December 31, 2017, the Secretary shall adjust the $6,000 amount under clause (ii) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter beginning July 1, 2016, and any increase under this paragraph that is not a multiple

of $500 shall be rounded to the next lowest multiple of $500.

(iv) Special rule for application of limitation on accruals for certain plans

In the case of a plan described in subparagraph (A)(ii) which is a defined benefit plan (as defined in section 414(j)), the limitation under clause (ii) shall apply to the actuarial present value of the aggregate amount of length of service awards accruing with respect to any year of service. Such actuarial present value with respect to any year shall be calculated using reasonable actuarial assumptions and methods, assuming payment will be made under the most valuable form of payment under the plan with payment commencing at the later of the earliest age at which unreduced benefits are payable under the plan or the participant's age at the time of the calculation.

(C) Qualified services

For purposes of this paragraph, the term ''qualified services'' means fire fighting and prevention services, emergency medical services, and ambulance services.

(D) Certain voluntary early retirement incentive plans

(i) In general

If an applicable voluntary early retirement incentive plan—

(I) makes payments or supplements as an early retirement benefit, a retirement-type subsidy, or a benefit described in the last sentence of section 411(a)(9), and

(II) such payments or supplements are made in coordination with a defined benefit plan which is described in section 401(a) and includes a trust exempt from tax under section 501(a) and which is maintained by an eligible employer described in paragraph (1)(A) or by an education association described in clause (ii)(II),

such applicable plan shall be treated for purposes of subparagraph (A)(i) as a bona fide severance pay plan with respect to such payments or supplements to the extent such payments or supplements could otherwise have been provided under such defined benefit plan (determined as if section 411 applied to such defined benefit plan).

(ii) Applicable voluntary early retirement incentive plan

For purposes of this subparagraph, the term ''applicable voluntary early retirement incentive plan'' means a voluntary early retirement incentive plan maintained by—

(I) a local educational agency (as defined in section 8101 of the Elementary and Secondary Education Act of 1965), or

(II) an education association which principally represents employees of 1 or more agencies described in subclause (I) and which is described in section 501(c)(5) or (6) and exempt from tax under section 501(a).

(12) Exception for nonelective deferred compensation of nonemployees

(A) In general

This section shall not apply to nonelective deferred compensation attributable to services not performed as an employee.

(B) Nonelective deferred compensation

For purposes of subparagraph (A), deferred compensation shall be treated as nonelective only if all individuals (other than those who have not satisfied any applicable initial service requirement) with the same relationship to the payor are covered under the same plan with no individual variations or options under the plan.

(13) Special rule for churches

The term ''eligible employer'' shall not include a church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).

(14) Treatment of qualified governmental excess benefit arrangements

Subsections (b)(2) and (c)(1) shall not apply to any qualified governmental excess benefit arrangement (as defined in section 415(m)(3)), and benefits provided under such an arrangement shall not be taken into account in determining whether any other plan is an eligible deferred compensation plan.

(15) Applicable dollar amount

(A) In general

The applicable dollar amount is $15,000.

(B) Cost-of-living adjustments

In the case of taxable years beginning after December 31, 2006, the Secretary shall adjust the $15,000 amount under subparagraph (A) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter beginning July 1, 2005, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500.

(16) Rollover amounts

(A) General rule

In the case of an eligible deferred compensation plan established and maintained by an employer described in subsection (e)(1)(A), if—

(i) any portion of the balance to the credit of an employee in such plan is paid to such employee in an eligible rollover distribution (within the meaning of section 402(c)(4)),

(ii) the employee transfers any portion of the property such employee receives in such distribution to an eligible retirement plan described in section 402(c)(8)(B), and

(iii) in the case of a distribution of property other than money, the amount so transferred consists of the property distributed,

then such distribution (to the extent so transferred) shall not be includible in gross income for the taxable year in which paid.

(B) Certain rules made applicable

The rules of paragraphs (2) through (7), (9), and (11) of section 402(c) and section 402(f) shall apply for purposes of subparagraph (A).

(C) Reporting

Rollovers under this paragraph shall be reported to the Secretary in the same manner as rollovers from qualified retirement plans (as defined in section 4974(c)).

(17) Trustee-to-trustee transfers to purchase permissive service credit

No amount shall be includible in gross income by reason of a direct trustee-to-trustee transfer to a defined benefit governmental plan (as defined in section 414(d)) if such transfer is—

(A) for the purchase of permissive service credit (as defined in section 415(n)(3)(A)) under such plan, or

(B) a repayment to which section 415 does not apply by reason of subsection (k)(3) thereof.

(18) Coordination with catch-up contributions for individuals age 50 or older

In the case of an individual who is an eligible participant (as defined by section 414(v)) and who is a participant in an eligible deferred compensation plan of an employer described in paragraph (1)(A), subsections (b)(3) and (c) shall be applied by substituting for the amount otherwise determined under the applicable subsection the greater of—

(A) the sum of—

(i) the plan ceiling established for purposes of subsection (b)(2) (without regard to subsection (b)(3)), plus

(ii) the applicable dollar amount for the taxable year determined under section 414(v)(2)(B)(i), or

(B) the amount determined under the applicable subsection (without regard to this paragraph).

(f) Tax treatment of participants where plan or arrangement of employer is not eligible

(1) In general

In the case of a plan of an eligible employer providing for a deferral of compensation, if such plan is not an eligible deferred compensation plan, then—

(A) the compensation shall be included in the gross income of the participant or beneficiary for the 1st taxable year in which there is no substantial risk of forfeiture of the rights to such compensation, and

(B) the tax treatment of any amount made available under the plan to a participant or beneficiary shall be determined under section 72 (relating to annuities, etc.).

(2) Exceptions

Paragraph (1) shall not apply to—

(A) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

(B) an annuity plan or contract described in section 403,

(C) that portion of any plan which consists of a transfer of property described in section 83,

(D) that portion of any plan which consists of a trust to which section 402(b) applies,

(E) a qualified governmental excess benefit arrangement described in section 415(m), and

(F) that portion of any applicable employment retention plan described in paragraph (4) with respect to any participant.

(3) Definitions

For purposes of this subsection—

(A) Plan includes arrangements, etc.

The term ''plan'' includes any agreement or arrangement.

(B) Substantial risk of forfeiture

The rights of a person to compensation are subject to a substantial risk of forfeiture if such person's rights to such compensation are conditioned upon the future performance of substantial services by any individual.

(4) Employment retention plans

For purposes of paragraph (2)(F)—

(A) In general

The portion of an applicable employment retention plan described in this paragraph with respect to any participant is that portion of the plan which provides benefits payable to the participant not in excess of twice the applicable dollar limit determined under subsection (e)(15).

(B) Other rules

(i) Limitation

Paragraph (2)(F) shall only apply to the portion of the plan described in subparagraph (A) for years preceding the year in which such portion is paid or otherwise made available to the participant.

(ii) Treatment

A plan shall not be treated for purposes of this title as providing for the deferral of compensation for any year with respect to the portion of the plan described in subparagraph (A).

(C) Applicable employment retention plan

The term ''applicable employment retention plan'' means an employment retention plan maintained by—

(i) a local educational agency (as defined in section 8101 of the Elementary and Secondary Education Act of 1965 (20 U.S.C. 7801)), or

(ii) an education association which principally represents employees of 1 or more agencies described in clause (i) and which is described in section 501(c)(5) or (6) and exempt from taxation under section 501(a).

(D) Employment retention plan

The term ''employment retention plan'' means a plan to pay, upon termination of employment, compensation to an employee of a local educational agency or education association described in subparagraph (C) for purposes of—

(i) retaining the services of the employee, or

(ii) rewarding such employee for the employee's service with 1 or more such agencies or associations.

(g) Governmental plans must maintain set-asides for exclusive benefit of participants

(1) In general

A plan maintained by an eligible employer described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

(2) Taxability of trusts and participants

For purposes of this title—

(A) a trust described in paragraph (1) shall be treated as an organization exempt from taxation under section 501(a), and

(B) notwithstanding any other provision of this title, amounts in the trust shall be includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

(3) Custodial accounts and contracts

For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).

(4) Death benefits under USERRA-qualified active military service

A plan described in paragraph (1) shall not be treated as an eligible deferred compensation plan unless such plan meets the requirements of section 401(a)(37).

(Added Pub. L. 95–600, title I, §131(a), Nov. 6, 1978, 92 Stat. 2779; amended Pub. L. 96–222, title I, §101(a)(4), Apr. 1, 1980, 94 Stat. 196; Pub. L. 98–369, div. A, title IV, §491(d)(33), July 18, 1984, 98 Stat. 851; Pub. L. 99–514, title XI, §1107(a), Oct. 22, 1986, 100 Stat. 2426; Pub. L. 100–647, title I, §1011(e)(1), (2), (9), (10), title VI, §§6064(a)–(c), 6071(c), Nov. 10, 1988, 102 Stat. 3460, 3461, 3700, 3701, 3705; Pub. L. 101–239, title VII, §§7811(g)(4), (5), 7816(j), Dec. 19, 1989, 103 Stat. 2409, 2421; Pub. L. 102–318, title V, §521(b)(26), July 3, 1992, 106 Stat. 312; Pub. L. 104–188, title I, §§1421(b)(3)(C), 1444(b)(2), (3), 1447(a), (b), 1448(a), (b), 1458(a), Aug. 20, 1996, 110 Stat. 1796, 1810, 1812, 1813, 1819; Pub. L. 105–34, title X, §1071(a)(2), Aug. 5, 1997, 111 Stat. 948; Pub. L. 107–16, title VI, §§611(d)(3)(B), (e), 615(a), 632(c)(1), 641(a)(1)(A)–(C), 646(a)(3), 647(b), 648(b), 649(a), (b), June 7, 2001, 115 Stat. 98, 102, 115, 118, 119, 126–128; Pub. L. 107–147, title IV, §411(*o*)(9), (p)(5), Mar. 9, 2002, 116 Stat. 49, 51; Pub. L. 109–280, title VIII, §§829(a)(4), 845(b)(3), title XI, §1104(a)(1), (b), Aug. 17, 2006, 120 Stat. 1002, 1015, 1058, 1059; Pub. L. 110–245, title I, §104(c)(3), June 17, 2008, 122 Stat. 1627; Pub. L. 113–295, div. A, title II, §221(a)(57)(H), Dec. 19, 2014, 128 Stat. 4047; Pub. L. 114–95, title IX, §9215(uu)(2), Dec. 10, 2015, 129 Stat. 2183; Pub. L. 115–97, title I, §13612(a)–(c), Dec. 22, 2017, 131 Stat. 2165; Pub. L. 115–141, div. U, title IV, §401(a)(112), Mar. 23, 2018, 132 Stat. 1189; Pub. L. 116–94, div. M, §104(b), div. O, title I, §109(d), Dec. 20, 2019, 133 Stat. 3095, 3151.)

INFLATION ADJUSTED ITEMS FOR CERTAIN YEARS

For inflation adjustment of certain items in this section, see Internal Revenue Notices listed in a table under section 401 of this title.

REFERENCES IN TEXT

Section 8101 of the Elementary and Secondary Education Act of 1965, referred to in subsec. (e)(11)(D)(ii)(I), is classified to section 7801 of Title 20, Education.

AMENDMENTS

2019—Subsec. (d)(1)(A)(i). Pub. L. 116–94, §104(b), inserted ''(in the case of a plan maintained by an employer described in subsection (e)(1)(A), age 59½)'' before comma at end.

Subsec. (d)(1)(A)(iv). Pub. L. 116–94, §109(d)(1), added cl. (iv).

Subsec. (d)(1)(D). Pub. L. 116–94, §109(d)(2), added subpar. (D).

2018—Subsec. (f)(4)(C)(i). Pub. L. 115–141 substituted ''section 8101'' for ''section 9101'' and ''(20 U.S.C. 7801)),'' for ''(20 U.S.C. 7801),''.

2017—Subsec. (e)(11)(B)(ii). Pub. L. 115–97, §13612(a), substituted ''$6,000'' for ''$3,000''.

Subsec. (e)(11)(B)(iii). Pub. L. 115–97, §13612(b), added cl. (iii).

Subsec. (e)(11)(B)(iv). Pub. L. 115–97, §13612(c), added cl. (iv).

2015—Subsec. (e)(11)(D)(ii)(I). Pub. L. 114–95 substituted ''section 8101 of the Elementary and Secondary Education Act of 1965'' for ''section 9101 of the Elementary and Secondary Education Act of 1965 (20 U.S.C. 7801)''.

2014—Subsec. (e)(15)(A). Pub. L. 113–295 substituted ''is $15,000.'' for ''shall be the amount determined in accordance with the following table:'' and struck out table at end listing applicable dollar amounts for taxable years beginning in 2002.

2008—Subsec. (g)(4). Pub. L. 110–245 added par. (4).

2006—Subsec. (a)(3). Pub. L. 109–280, §845(b)(3), added par. (3).

Subsec. (e)(11)(D). Pub. L. 109–280, §1104(a)(1), added subpar. (D).

Subsec. (e)(16)(B). Pub. L. 109–280, §829(a)(4), substituted '', (9), and (11)'' for ''and (9)''.

Subsec. (f)(2)(F). Pub. L. 109–280, §1104(b)(1), added subpar. (F).

Subsec. (f)(4). Pub. L. 109–280, §1104(b)(2), added par. (4).

2002—Subsec. (e)(5). Pub. L. 107–147, §411(p)(5), reenacted heading without change and amended text generally. Prior to amendment, text read as follows: ''The term 'includible compensation' means compensation for service performed for the employer which (taking into account the provisions of this section and other provisions of this chapter) is currently includible in gross income.''

Subsec. (e)(18). Pub. L. 107–147, §411(*o*)(9), added par. (18).

2001—Subsec. (a). Pub. L. 107–16, §649(b)(1), reenacted heading without change and amended text of subsec. (a) generally. Prior to amendment, text read as follows: ''In the case of a participant in an eligible deferred compensation plan, any amount of compensation deferred under the plan, and any income attributable to the amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or other beneficiary.''

Subsec. (b)(2). Pub. L. 107–16, §641(a)(1)(B), inserted ''(other than rollover amounts)'' after ''taxable year'' in introductory provisions.

Subsec. (b)(2)(A). Pub. L. 107–16, §611(e)(1)(A), substituted ''the applicable dollar amount'' for ''$7,500''.

Subsec. (b)(2)(B). Pub. L. 107–16, §632(c)(1), substituted ''100 percent'' for ''33⅓ percent''.

Subsec. (b)(3)(A). Pub. L. 107–16, §611(e)(1)(B), substituted ''twice the dollar amount in effect under subsection (b)(2)(A)'' for ''$15,000''.

Subsec. (c). Pub. L. 107–16, § 615(a), amended heading and text of subsec. (c) generally, substituting present provisions for provisions which stated that the maximum amount of compensation that an individual could defer under subsec. (a) during any taxable year could not exceed the applicable dollar amount, as modified by any adjustment provided under subsec. (b)(3), and provided for coordination with certain other deferrals.

Subsec. (c)(1). Pub. L. 107–16, § 611(e)(1)(A), substituted ''the applicable dollar amount'' for ''$7,500''.

Subsec. (c)(2). Pub. L. 107–16, § 611(d)(3)(B), substituted ''402(g)(7)(A)(iii)'' for ''402(g)(8)(A)(iii)'' in concluding provisions.

Subsec. (d)(1). Pub. L. 107–16, § 641(a)(1)(C), added subpar. (C) and concluding provisions.

Subsec. (d)(1)(A)(ii). Pub. L. 107–16, § 646(a)(3), substituted ''has a severance from employment'' for ''is separated from service''.

Subsec. (d)(2). Pub. L. 107–16, § 649(a), reenacted heading without change and amended text of par. (2) generally, substituting present provisions for provisions which stated that a plan would meet the minimum distribution requirements of this par. if plan met the requirements of section 401(a)(9), if plan met additional distribution requirements in the case of a deceased participant, and if any distribution payable over a period of more than 1 year would only be made in substantially nonincreasing amounts.

Subsec. (d)(3). Pub. L. 107–16, § 649(b)(2)(B), added par. (3).

Subsec. (e)(9). Pub. L. 107–16, § 649(b)(2)(A), in heading substituted ''Benefits of tax exempt organization plans not treated as made available by reason of certain elections, etc.'' for ''Benefits not treated as made available by reason of certain elections, etc.'' and inserted introductory provisions.

Subsec. (e)(9)(A)(i). Pub. L. 107–16, § 648(b), substituted ''the portion of such amount which is not attributable to rollover contributions (as defined in section 411(a)(11)(D))'' for ''such amount''.

Subsec. (e)(15). Pub. L. 107–16, § 611(e)(2), amended heading and text of par. (15) generally. Prior to amendment, text read as follows: ''The Secretary shall adjust the $7,500 amount specified in subsections (b)(2) and (c)(1) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1994, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500.''

Subsec. (e)(16). Pub. L. 107–16, § 641(a)(1)(A), added par. (16).

Subsec. (e)(17). Pub. L. 107–16, § 647(b), added par. (17).

1997—Subsec. (e)(9)(A). Pub. L. 105–34 substituted ''dollar limit'' for ''$3,500'' in heading and ''the dollar limit under section 411(a)(11)(A)'' for ''$3,500'' in cl. (i).

1996—Subsec. (b)(6). Pub. L. 104–188, § 1448(b), inserted ''except as provided in subsection (g),'' before ''which provides that'' in introductory provisions.

Subsec. (c)(2)(B)(i). Pub. L. 104–188, § 1421(b)(3)(C), substituted ''section 402(h)(1)(B) or (k)'' for ''section 402(h)(1)(B)''.

Subsec. (e)(9). Pub. L. 104–188, § 1447(a), amended par. (9) generally. Prior to amendment, par. (9) read as follows: ''BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS.—If—

''(A) the total amount payable to a participant under the plan does not exceed $3,500, and

''(B) no additional amounts may be deferred under the plan with respect to the participant,

the amount payable to the participant under the plan shall not be treated as made available merely because such participant may elect to receive a lump sum payable after separation from service and within 60 days of the election.''

Subsec. (e)(11). Pub. L. 104–188, § 1458(a), amended par. (11) generally. Prior to amendment, par. (11) read as follows: ''CERTAIN PLANS EXCEPTED.—Any bona fide vacation leave, sick leave, compensatory time, severance pay, disability pay, or death benefit plan shall be treated as a plan not providing for the deferral of compensation.''

Subsec. (e)(14). Pub. L. 104–188, § 1444(b)(2), added par. (14).

Subsec. (e)(15). Pub. L. 104–188, § 1447(b), added par. (15).

Subsec. (f)(2)(E). Pub. L. 104–188, § 1444(b)(3), added subpar. (E).

Subsec. (g). Pub. L. 104–188, § 1448(a), added subsec. (g).

1992—Subsec. (c)(2)(B)(i). Pub. L. 102–318 substituted ''402(e)(3)'' for ''402(a)(8)''.

1989—Subsec. (d)(1)(A)(iii). Pub. L. 101–239, § 7811(g)(4), substituted '', and'' for period at end.

Subsec. (d)(2)(B)(i)(I). Pub. L. 101–239, § 7811(g)(5), inserted ''and'' at end.

Subsec. (e)(13). Pub. L. 101–239, § 7816(j), substituted ''Special rule for churches'' for ''Exception for church plans'' in heading and amended text generally. Prior to amendment, text read as follows: ''The term 'eligible deferred compensation plan' shall not include a plan maintained by a church for church employees. For purposes of this paragraph, the term 'church' has the meaning given such term by section 3121(w)(3)(A), including a qualified church-controlled organization (as defined in section 3121(w)(3)(B)).''

1988—Subsec. (c)(2). Pub. L. 100–647, § 1011(e)(1), struck out ''and paragraphs (2) and (3) of subsection (b)'' after ''of this subsection''.

Pub. L. 100–647, § 6071(c), substituted ''rural cooperative plan'' for ''rural electric cooperative plan'' in last sentence.

Subsec. (d)(1)(A). Pub. L. 100–647, § 1011(e)(2), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''the plan provides that amounts payable under the plan will be made available to participants or other beneficiaries not earlier than when the participant is separated from service with the employer or is faced with an unforeseeable emergency (determined in the manner prescribed by the Secretary by regulation), and''.

Subsec. (d)(2)(B)(i)(I). Pub. L. 100–647, § 1011(e)(10), amended subcl. (I) generally. Prior to amendment, subcl. (I) read as follows: ''at least ⅔ of the total amount payable with respect to the participant will be paid during the life expectancy of such participant (determined as of the commencement of the distribution), and''.

Subsec. (d)(10). Pub. L. 100–647, § 6064(a)(2), amended subsec. (d), as in effect on the day before the date of enactment of Pub. L. 99–514 (Oct. 22, 1986), by adding par. (10) reading as follows: ''CERTAIN PLANS EXCEPTED.—Any bona fide vacation leave, sick leave, compensatory time, severance pay, disability pay, or death benefit plan shall be treated as a plan not providing for the deferral of compensation.''

Subsec. (d)(11). Pub. L. 100–647, § 6064(b)(2), amended subsec. (d), as in effect on the day before the date of enactment of Pub. L. 99–514 (Oct. 22, 1986), by adding par. (11) reading as follows: ''EXCEPTION FOR NONELECTIVE DEFERRED COMPENSATION OF NONEMPLOYEES.—

''(A) IN GENERAL.—This section shall not apply to nonelective deferred compensation attributable to services not performed as an employee.

''(B) NONELECTIVE DEFERRED COMPENSATION.—For purposes of subparagraph (a), deferred compensation shall be treated as nonelective only if all individuals (other than those who have not satisfied any applicable initial service requirement) with the same relationship to the payor are covered under the same plan with no individual variations or options under the plan.''

Subsec. (e)(9). Pub. L. 100–647, § 1011(e)(9), inserted ''after separation from service and'' after ''lump sum payable'' in concluding provisions.

Subsec. (e)(11). Pub. L. 100–647, § 6064(a)(1), added par. (11).

Subsec. (e)(12). Pub. L. 100–647, § 6064(b)(1), added par. (12).

Subsec. (e)(13). Pub. L. 100–647, § 6064(c), added par. (13).

1986—Pub. L. 99–514 amended section generally, substituting ''Deferred compensation plans of State and local governments and tax-exempt organizations'' for ''Deferred compensation plans with respect to service for State and local governments'' as section catchline and revising and restating as subsecs. (a) to (c), (e), and (f) provisions formerly contained in subsecs. (a) to (e) and adding provisions comprising subsec. (d).

1984—Subsec. (e)(2). Pub. L. 98–369, § 491(d)(33), struck out subpar. (C) which provided that par. (1) of this subsection not apply to a qualified bond purchase plan described in section 405(a), and redesignated subpars. (D) and (E) as (C) and (D), respectively.

1980—Subsec. (d)(9)(B). Pub. L. 96–222 in cl. (i) struck out ''described in section 501(c)(12)'' after ''any organization'' and substituted ''electric service on a mutual or cooperative basis'' for ''electric service'' and in cl. (ii) substituted ''paragraph (4) or (6) of section 501(a)'' for ''section 501(c)(6)'' and ''at least 80 percent of the members'' for ''all the members''.

EFFECTIVE DATE OF 2019 AMENDMENT

Amendment by section 104(b) of Pub. L. 116–94 applicable to plan years beginning after Dec. 31, 2019, see section 104(c) of Pub. L. 116–94, set out as a note under section 401 of this title.

Amendment by section 109(d) of Pub. L. 116–94 applicable to plan years beginning after Dec. 31, 2019, see section 109(e) of Pub. L. 116–94, set out as a note under section 401 of this title.

EFFECTIVE DATE OF 2017 AMENDMENT

Pub. L. 115–97, title I, § 13612(d), Dec. 22, 2017, 131 Stat. 2166, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2017.''

EFFECTIVE DATE OF 2015 AMENDMENT

Amendment by Pub. L. 114–95 effective Dec. 10, 2015, except with respect to certain noncompetitive programs and competitive programs, see section 5 of Pub. L. 114–95, set out as a note under section 6301 of Title 20, Education.

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 2008 AMENDMENT

Amendment by Pub. L. 110–245 applicable with respect to deaths and disabilities occurring on or after Jan. 1, 2007, see section 104(d)(1) of Pub. L. 110–245, set out as a note under section 401 of this title.

EFFECTIVE DATE OF 2006 AMENDMENT

Amendment by section 829(a)(4) of Pub. L. 109–280 applicable to distributions after Dec. 31, 2006, see section 829(b) of Pub. L. 109–280, set out as a note under section 402 of this title.

Amendment by section 845(b)(3) of Pub. L. 109–280 applicable to distributions in taxable years beginning after Dec. 31, 2006, see section 845(c) of Pub. L. 109–280, set out as a note under section 402 of this title.

Pub. L. 109–280, title XI, § 1104(d), Aug. 17, 2006, 120 Stat. 1060, as amended by Pub. L. 110–458, title I, § 111(a), Dec. 23, 2008, 122 Stat. 5113, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section and sections 623 and 1002 of Title 29, Labor] shall take effect on the date of the enactment of this Act [Aug. 17, 2006].

''(2) TAX AMENDMENTS.—The amendments made by subsections (a)(1) and (b) [amending this section] shall apply to taxable years ending after the date of the enactment of this Act [Aug. 17, 2006].

''(3) ERISA AMENDMENTS.—The amendment made by subsection (c) [amending section 1002 of Title 29, Labor] shall apply to plan years ending after the date of the enactment of this Act [Aug. 17, 2006].

''(4) CONSTRUCTION.—Nothing in the amendments made by this section [amending this section and sections 623 and 1002 of Title 29, Labor] shall alter or affect the construction of the Internal Revenue Code of 1986, the Employee Retirement Income Security Act of 1974 [29 U.S.C. 1001 et seq.], or the Age Discrimination in Employment Act of 1967 [29 U.S.C. 621 et seq.] as applied to any plan, arrangement, or conduct to which such amendments do not apply.''

EFFECTIVE DATE OF 2002 AMENDMENT

Amendment by Pub. L. 107–147 effective as if included in the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107–16, to which such amendment relates, see section 411(x) of Pub. L. 107–147, set out as a note under section 25B of this title.

EFFECTIVE DATE OF 2001 AMENDMENT

Amendment by section 611(d)(3)(B), (e) of Pub. L. 107–16 applicable to years beginning after Dec. 31, 2001, see section 611(i)(1) of Pub. L. 107–16, set out as a note under section 415 of this title.

Pub. L. 107–16, title VI, § 615(b), June 7, 2001, 115 Stat. 102, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to years beginning after December 31, 2001.''

Pub. L. 107–16, title VI, § 632(c)(2), June 7, 2001, 115 Stat. 115, provided that: ''The amendment made by this subsection [amending this section] shall apply to years beginning after December 31, 2001.''

Amendment by section 641(a)(1)(A)–(C) of Pub. L. 107–16 applicable to distributions after Dec. 31, 2001, see section 641(f)(1) of Pub. L. 107–16, set out as a note under section 402 of this title.

Amendment by section 646(a)(3) of Pub. L. 107–16 applicable to distributions after Dec. 31, 2001, see section 646(b) of Pub. L. 107–16, set out as a note under section 401 of this title.

Amendment by section 647(b) of Pub. L. 107–16 applicable to trustee-to-trustee transfers after Dec. 31, 2001, see section 647(c) of Pub. L. 107–16, set out as a note under section 403 of this title.

Amendment by section 648(b) of Pub. L. 107–16 applicable to distributions after Dec. 31, 2001, see section 648(c) of Pub. L. 107–16, set out as a note under section 411 of this title.

Pub. L. 107–16, title VI, § 649(c), June 7, 2001, 115 Stat. 128, provided that: ''The amendments made by subsections (a) and (b) [amending this section] shall apply to distributions after December 31, 2001.''

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105–34 applicable to plan years beginning after Aug. 5, 1997, see section 1071(c) of Pub. L. 105–34, set out as a note under section 411 of this title.

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by section 1421(b)(3)(C) of Pub. L. 104–188 applicable to taxable years beginning after Dec. 31, 1996, see section 1421(e) of Pub. L. 104–188, set out as a note under section 72 of this title.

Amendment by section 1444(b)(2), (3) of Pub. L. 104–188 applicable to years beginning after Dec. 31, 1994, see section 1444(e) of Pub. L. 104–188, set out as a note under section 415 of this title.

Pub. L. 104–188, title I, § 1447(c), Aug. 20, 1996, 110 Stat. 1812, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1996.''

Pub. L. 104–188, title I, § 1448(c), Aug. 20, 1996, 110 Stat. 1813, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to assets and income described in section 457(b)(6) of the Internal Revenue Code of 1986 held by a plan on and after the date of the enactment of this Act [Aug. 20, 1996].

''(2) TRANSITION RULE.—In the case of a plan in existence on the date of the enactment of this Act, a trust

need not be established by reason of the amendments made by this section before January 1, 1999.''

Pub. L. 104–188, title I, §1458(c)(1), Aug. 20, 1996, 110 Stat. 1820, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to accruals of length of service awards after December 31, 1996.''

EFFECTIVE DATE OF 1992 AMENDMENT

Amendment by Pub. L. 102–318 applicable to distributions after Dec. 31, 1992, see section 521(e) of Pub. L. 102–318, set out as a note under section 402 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by Pub. L. 101–239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 7817 of Pub. L. 101–239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Pub. L. 100–647, title I, §1011(e)(9), Nov. 10, 1988, 102 Stat. 3461, provided that the amendment made by that section is effective for years beginning after Dec. 31, 1988.

Amendment by section 1011(e)(1), (2), (10) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Pub. L. 100–647, title VI, §6064(d), Nov. 10, 1988, 102 Stat. 3701, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1987.

''(2) EXCEPTION FOR CERTAIN COLLECTIVELY BARGAINED PLANS.—

''(A) IN GENERAL.—Section 457 of the 1986 Code (as in effect before and after the amendments made by section 1107 of the Reform Act [Pub. L. 99–514]) shall not apply to nonelective deferred compensation provided under a plan in existence on December 31, 1987, and maintained pursuant to a collective bargaining agreement.

''(B) NONELECTIVE PLAN.—For purposes of this paragraph, a nonelective plan is a plan which covers a broad group of employees and under which the covered employees earn nonelective deferred compensation under a definite, fixed and uniform benefit formula.

''(C) TERMINATION.—This paragraph shall cease to apply to a plan as of the effective date of the first material modification of the plan agreed to after December 31, 1987.

''(3) TREATMENT OF CERTAIN NONELECTIVE DEFERRED COMPENSATION.—Section 457 of the 1986 Code shall not apply to amounts deferred under a nonelective deferred compensation plan maintained by an eligible employer described in section 457(e)(1)(A) of the 1986 Code (as in effect after the Reform Act [Pub. L. 99–514])—

''(A) if such amounts were deferred from periods before July 14, 1988, or

''(B) if—

''(i) such amounts are deferred from periods on or after such date pursuant to an agreement which—

''(I) was in writing on such date, and

''(II) on such date provides for a deferral for each taxable year covered by the agreement of a fixed amount or of an amount determined pursuant to a fixed formula, and

''(ii) the individual with respect to whom the deferral is made was covered under such agreement on such date.

Subparagraph (B) shall not apply to any taxable year ending after the date on which any modification of the amount or formula described in subparagraph (B)(i)(II) agreed to in writing before January 1, 1989, is effective. The preceding sentence shall not apply to a modification agreed to in writing before January 1, 1989, which does not increase any benefit of a participant. Amounts described in the first sentence of this paragraph shall be taken into account for purposes of applying section 457 of the 1986 Code to other amounts deferred under any eligible deferred compensation plan.

''(4) STUDY.—The Secretary of the Treasury or his delegate shall conduct a study on the tax treatment of deferred compensation paid by State and local governments and tax-exempt organizations (including deferred compensation paid to independent contractors). Not later than January 1, 1990, the Secretary shall submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report on the study conducted under this paragraph together with such recommendations as he may deem advisable.''

[The due date for the report on the study referred to in section 6064(d)(4) of Pub. L. 100–647, set out above, extended to Jan. 1, 1992, by Pub. L. 101–508, title XI, §11831(b), Nov. 5, 1990, 104 Stat. 1388–559.]

Amendment by section 6071(c) of Pub. L. 100–647 applicable to taxable years beginning after Nov. 10, 1988, see section 6071(d) of Pub. L. 100–647, set out as a note under section 401 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99–514, title XI, §1107(c), Oct. 22, 1986, 100 Stat. 2430, as amended by Pub. L. 100–647, title I, §1011(e)(6), (7), Nov. 10, 1988, 102 Stat. 3461, provided that:

''(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1988.

''(2) TRANSFERS AND CASH-OUTS.—Paragraphs (9) and (10) of section 457(e) of the Internal Revenue Code of 1986 (as amended by this section) shall apply to taxable years beginning after December 31, 1986.

''(3) APPLICATION TO TAX-EXEMPT ORGANIZATIONS.—

''(A) IN GENERAL.—Except as provided in subparagraph (B), the application of section 457 of the Internal Revenue Code of 1986 by reason of the amendments made by this section to deferred compensation plans established and maintained by organizations exempt from tax shall apply to taxable years beginning after December 31, 1986.

''(B) EXISTING DEFERRALS AND ARRANGEMENTS.—Section 457 of such Code shall not apply to amounts deferred under a plan described in subparagraph (A) which—

''(i) were deferred from taxable years beginning before January 1, 1987, or

''(ii) are deferred from taxable years beginning after December 31, 1986, pursuant to an agreement which—

''(I) was in writing on August 16, 1986,

''(II) on such date provides for a deferral for each taxable year covered by the agreement of a fixed amount or of an amount determined pursuant to a fixed formula.

Clause (ii) shall not apply to any taxable year ending after the date on which any modification to the amount or formula described in subclause (II) is effective. Amounts described in the first sentence shall be taken into account for applying section 457 to other amounts deferred under any deferred compensation plan. This subparagraph shall only apply to individuals who were covered under the plan and agreement on August 16, 1986.

''(4) DEFERRED COMPENSATION PLANS FOR STATE JUDGES.—The amendments made by this section shall not apply to any qualified State judicial plan (as defined in section 131(c)(3)(B) of the Revenue Act of 1978 [set out as a note below] as amended by section 252 of the Tax Equity and Fiscal Responsibility Act of 1982).

''(5) SPECIAL RULE FOR CERTAIN DEFERRED COMPENSATION PLANS.—The amendments made by this section shall not apply—

''(A) to employees on August 16, 1986, of a nonprofit corporation organized under the laws of the State of

Alabama maintaining a deferred compensation plan with respect to which the Internal Revenue Service issued a ruling dated March 17, 1976, that the plan would not affect the tax-exempt status of the corporation, or

''(B) to to [sic] individuals eligible to participate on August 16, 1986, in a deferred compensation plan with respect to which a letter dated November 6, 1975, submitted the original plan to the Internal Revenue Service, an amendment was submitted on November 19, 1975, and the Internal Revenue Service responded with a letter dated December 24, 1975,

but only with respect to deferrals under such plan.''

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98–369 applicable to obligations issued after Dec. 31, 1983, see section 491(f)(1) of Pub. L. 98–369, set out as a note under section 62 of this title.

EFFECTIVE DATE OF 1980 AMENDMENT

Amendment by Pub. L. 96–222 effective, except as otherwise provided, as if it had been included in the provisions of the Revenue Act of 1978, Pub. L. 95–600, to which such amendment relates, see section 201 of Pub. L. 96–222, set out as a note under section 32 of this title.

EFFECTIVE DATE

Pub. L. 95–600, title I, § 131(c)(1), Nov. 6, 1978, 92 Stat. 2782, provided that: ''The amendments made by this section [enacting this section] shall apply to taxable years beginning after December 31, 1978.''

ELIGIBILITY FOR PARTICIPATION IN RETIREMENT PLANS

Pub. L. 109–280, title VIII, § 825, Aug. 17, 2006, 120 Stat. 999, provided that: ''An individual shall not be precluded from participating in an eligible deferred compensation plan by reason of having received a distribution under section 457(e)(9) of the Internal Revenue Code of 1986, as in effect prior to the enactment of the Small Business Job Protection Act of 1996 [Pub. L. 104–188, Aug. 20, 1996].''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1998

For provisions directing that if any amendments made by subtitle D [§§ 1401–1465] of title I of Pub. L. 104–188 require an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after Jan. 1, 1998, see section 1465 of Pub. L. 104–188, set out as a note under section 401 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1994

For provisions directing that if any amendments made by subtitle B [§§ 521–523] of title V of Pub. L. 102–318 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1994, see section 523 of Pub. L. 102–318, set out as a note under section 401 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1100–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

TRANSITIONAL RULES

Pub. L. 95–600, title I, § 131(c)(2), Nov. 6, 1978, 92 Stat. 2782, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(A) IN GENERAL.—In the case of any taxable year beginning after December 31, 1978, and before January 1, 1982—

''(i) any amount of compensation deferred under a plan of a State providing for a deferral of compensation (other than a plan described in section 457(e)(2) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]), and any income attributable to the amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or other beneficiary, but

''(ii) the maximum amount of the compensation of any one individual which may be excluded from gross income by reason of clause (i) and by reason of section 457(a) of such Code during any such taxable year shall not exceed the lesser of—

''(I) $7,500, or

''(II) 33⅓ percent of the participant's includible compensation.

''(B) APPLICATION OF CATCH-UP PROVISIONS IN CERTAIN CASES.—If, in the case of any participant for any taxable year, all of the plans are eligible State deferred compensation plans, then clause (ii) of subparagraph (A) of this paragraph shall be applied with the modification provided by paragraph (3) of section 457(b) of such Code.

''(C) APPLICATIONS OF CERTAIN COORDINATION PROVISIONS.—In applying clause (ii) of subparagraph (A) of this paragraph and section 403(b)(2)(A)(ii) of such Code, rules similar to the rules of section 457(c)(2) of such Code shall apply.

''(D) MEANING OF TERMS.—Except as otherwise provided in this paragraph, terms used in this paragraph shall have the same meaning as when used in section 457 of such Code.''

DEFERRED COMPENSATION PLANS FOR STATE JUDGES

Pub. L. 95–600, title I, § 131(c)(3), as added by Pub. L. 97–248, title II, § 252, Sept. 3, 1982, 96 Stat. 532, and amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(A) IN GENERAL.—The amendments made by this section [enacting this section and provisions set out as notes under this section] shall not apply to any qualified State judicial plan.

''(B) QUALIFIED STATE JUDICIAL PLAN.—For purposes of subparagraph (A), the term 'qualified State judicial plan' means any retirement plan of a State for the exclusive benefit of judges or their beneficiaries if—

''(i) such plan has been continuously in existence since December 31, 1978,

''(ii) under such plan, all judges eligible to benefit under the plan—

''(I) are required to participate, and

''(II) are required to contribute the same fixed percentage of their basic or regular rate of compensation as judge,

''(iii) under such plan, no judge has an option as to contributions or benefits the exercise of which would affect the amount of includible compensation,

''(iv) the retirement payments of a judge under the plan are a percentage of the compensation of judges of that State holding similar positions, and

''(v) the plan during any year does not pay benefits with respect to any participant which exceed the limitations of section 415(b) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954].''

§ 457A. Nonqualified deferred compensation from certain tax indifferent parties

(a) In general

Any compensation which is deferred under a nonqualified deferred compensation plan of a nonqualified entity shall be includible in gross income when there is no substantial risk of forfeiture of the rights to such compensation.

(b) Nonqualified entity

For purposes of this section, the term ''nonqualified entity'' means—

(1) any foreign corporation unless substantially all of its income is—

(A) effectively connected with the conduct of a trade or business in the United States, or

(B) subject to a comprehensive foreign income tax, and

(2) any partnership unless substantially all of its income is allocated to persons other than—

(A) foreign persons with respect to whom such income is not subject to a comprehensive foreign income tax, and

(B) organizations which are exempt from tax under this title.

(c) Determinability of amounts of compensation

(1) In general

If the amount of any compensation is not determinable at the time that such compensation is otherwise includible in gross income under subsection (a)—

(A) such amount shall be so includible in gross income when determinable, and

(B) the tax imposed under this chapter for the taxable year in which such compensation is includible in gross income shall be increased by the sum of—

(i) the amount of interest determined under paragraph (2), and

(ii) an amount equal to 20 percent of the amount of such compensation.

(2) Interest

For purposes of paragraph (1)(B)(i), the interest determined under this paragraph for any taxable year is the amount of interest at the underpayment rate under section 6621 plus 1 percentage point on the underpayments that would have occurred had the deferred compensation been includible in gross income for the taxable year in which first deferred or, if later, the first taxable year in which such deferred compensation is not subject to a substantial risk of forfeiture.

(d) Other definitions and special rules

For purposes of this section—

(1) Substantial risk of forfeiture

(A) In general

The rights of a person to compensation shall be treated as subject to a substantial risk of forfeiture only if such person's rights to such compensation are conditioned upon the future performance of substantial services by any individual.

(B) Exception for compensation based on gain recognized on an investment asset

(i) In general

To the extent provided in regulations prescribed by the Secretary, if compensation is determined solely by reference to the amount of gain recognized on the disposition of an investment asset, such compensation shall be treated as subject to a substantial risk of forfeiture until the date of such disposition.

(ii) Investment asset

For purposes of clause (i), the term ''investment asset'' means any single asset (other than an investment fund or similar entity)—

(I) acquired directly by an investment fund or similar entity,

(II) with respect to which such entity does not (nor does any person related to such entity) participate in the active management of such asset (or if such asset is an interest in an entity, in the active management of the activities of such entity), and

(III) substantially all of any gain on the disposition of which (other than such deferred compensation) is allocated to investors in such entity.

(iii) Coordination with special rule

Paragraph (3)(B) shall not apply to any compensation to which clause (i) applies.

(2) Comprehensive foreign income tax

The term ''comprehensive foreign income tax'' means, with respect to any foreign person, the income tax of a foreign country if—

(A) such person is eligible for the benefits of a comprehensive income tax treaty between such foreign country and the United States, or

(B) such person demonstrates to the satisfaction of the Secretary that such foreign country has a comprehensive income tax.

(3) Nonqualified deferred compensation plan

(A) In general

The term ''nonqualified deferred compensation plan'' has the meaning given such term under section 409A(d), except that such term shall include any plan that provides a right to compensation based on the appreciation in value of a specified number of equity units of the service recipient.

(B) Exception

Compensation shall not be treated as deferred for purposes of this section if the service provider receives payment of such compensation not later than 12 months after the end of the taxable year of the service recipient during which the right to the payment of such compensation is no longer subject to a substantial risk of forfeiture.

(4) Exception for certain compensation with respect to effectively connected income

In the case of a foreign corporation with income which is taxable under section 882, this section shall not apply to compensation which, had such compensation been paid in cash on the date that such compensation ceased to be subject to a substantial risk of forfeiture, would have been deductible by such foreign corporation against such income.

(5) Application of rules

Rules similar to the rules of paragraphs (5) and (6) of section 409A(d) shall apply.

(e) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations disregarding a substantial risk of forfeiture in cases where necessary to carry out the purposes of this section.

(Added Pub. L. 110–343, div. C, title VIII, § 801(a), Oct. 3, 2008, 122 Stat. 3929; amended Pub. L. 115–141, div. U, title IV, § 401(a)(113), Mar. 23, 2018, 132 Stat. 1189.)

AMENDMENTS

2018—Subsec. (d)(4). Pub. L. 115–141 substituted ''case of a foreign'' for ''case a foreign'' and ''been paid'' for ''had been paid''.

EFFECTIVE DATE

Pub. L. 110–343, div. C, title VIII, § 801(d), Oct. 3, 2008, 122 Stat. 3931, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting this section and amending section 26 of this title] shall apply to amounts deferred which are attributable to services performed after December 31, 2008.

''(2) APPLICATION TO EXISTING DEFERRALS.—In the case of any amount deferred to which the amendments made by this section do not apply solely by reason of the fact that the amount is attributable to services performed before January 1, 2009, to the extent such amount is not includible in gross income in a taxable year beginning before 2018, such amounts shall be includible in gross income in the later of—

''(A) the last taxable year beginning before 2018, or

''(B) the taxable year in which there is no substantial risk of forfeiture of the rights to such compensation (determined in the same manner as determined for purposes of section 457A of the Internal Revenue Code of 1986, as added by this section).

''(3) ACCELERATED PAYMENTS.—No later than 120 days after the date of the enactment of this Act [Oct. 3, 2008], the Secretary shall issue guidance providing a limited period of time during which a nonqualified deferred compensation arrangement attributable to services performed on or before December 31, 2008, may, without violating the requirements of section 409A(a) of the Internal Revenue Code of 1986, be amended to conform the date of distribution to the date the amounts are required to be included in income.

''(4) CERTAIN BACK-TO-BACK ARRANGEMENTS.—If the taxpayer is also a service recipient and maintains one or more nonqualified deferred compensation arrangements for its service providers under which any amount is attributable to services performed on or before December 31, 2008, the guidance issued under paragraph (4) shall permit such arrangements to be amended to conform the dates of distribution under such arrangement to the date amounts are required to be included in the income of such taxpayer under this subsection.

''(5) ACCELERATED PAYMENT NOT TREATED AS MATERIAL MODIFICATION.—Any amendment to a nonqualified deferred compensation arrangement made pursuant to paragraph (4) or (5) shall not be treated as a material modification of the arrangement for purposes of section 409A of the Internal Revenue Code of 1986.''

§ 458. Magazines, paperbacks, and records returned after the close of the taxable year

(a) Exclusion from gross income

A taxpayer who is on an accrual method of accounting may elect not to include in the gross income for the taxable year the income attributable to the qualified sale of any magazine, paperback, or record which is returned to the taxpayer before the close of the merchandise return period.

(b) Definitions and special rules

For purposes of this section—

(1) Magazine

The term ''magazine'' includes any other periodical.

(2) Paperback

The term ''paperback'' means any book which has a flexible outer cover and the pages of which are affixed directly to such outer cover. Such term does not include a magazine.

(3) Record

The term ''record'' means a disc, tape, or similar object on which musical, spoken, or other sounds are recorded.

(4) Separate application with respect to magazines, paperbacks, and records

If a taxpayer makes qualified sales of more than one category of merchandise in connection with the same trade or business, this section shall be applied as if the qualified sales of each such category were made in connection with a separate trade or business. For purposes of the preceding sentence, magazines, paperbacks, and records shall each be treated as a separate category of merchandise.

(5) Qualified sale

A sale of a magazine, paperback, or record is a qualified sale if—

(A) at the time of sale, the taxpayer has a legal obligation to adjust the sales price of such magazine, paperback, or record if it is not resold, and

(B) the sales price of such magazine, paperback, or record is adjusted by the taxpayer because of a failure to resell it.

(6) Amount excluded

The amount excluded under this section with respect to any qualified sale shall be the lesser of—

(A) the amount covered by the legal obligation described in paragraph (5)(A), or

(B) the amount of the adjustment agreed to by the taxpayer before the close of the merchandise return period.

(7) Merchandise return period

(A) Except as provided in subparagraph (B), the term ''merchandise return period'' means, with respect to any taxable year—

(i) in the case of magazines, the period of 2 months and 15 days first occurring after the close of taxable year, or

(ii) in the case of paperbacks and records, the period of 4 months and 15 days first occurring after the close of the taxable year.

(B) The taxpayer may select a shorter period than the applicable period set forth in subparagraph (A).

(C) Any change in the merchandise return period shall be treated as a change in the method of accounting.

(8) Certain evidence may be substituted for physical return of merchandise

Under regulations prescribed by the Secretary, the taxpayer may substitute, for the physical return of magazines, paperbacks, or records required by subsection (a), certification or other evidence that the magazine, paperback, or record has not been resold and will not be resold if such evidence—

(A) is in the possession of the taxpayer at the close of the merchandise return period, and

(B) is satisfactory to the Secretary.

(9) Repurchase by the taxpayer not treated as resale

A repurchase by the taxpayer shall be treated as an adjustment of the sales price rather than as a resale.

(c) Qualified sales to which section applies

(1) Election of benefits

This section shall apply to qualified sales of magazines, paperbacks, or records, as the case may be, if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such sales are made. An election under this section may be made without the consent of the Secretary. The election shall be made in such manner as the Secretary may by regulations prescribe and shall be made for any taxable year not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof).

(2) Scope of election

An election made under this section shall apply to all qualified sales of magazines, paperbacks, or records, as the case may be, made in connection with the trade or business with respect to which the taxpayer has made the election.

(3) Period to which election applies

An election under this section shall be effective for the taxable year for which it is made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election.

(4) Treatment as method of accounting

Except to the extent inconsistent with the provisions of this section, for purposes of this subtitle, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

(d) 5-year spread of transitional adjustments for magazines

In applying section 481(c) with respect to any election under this section which applies to magazines, the period for taking into account any decrease in taxable income resulting from the application of section 481(a)(2) shall be the taxable year for which the election is made and the 4 succeeding taxable years.

(e) Suspense account for paperbacks and records

(1) In general

In the case of any election under this section which applies to paperbacks or records, in lieu of applying section 481, the taxpayer shall establish a suspense account for the trade or business for the taxable year for which the election is made.

(2) Initial opening balance

The opening balance of the account described in paragraph (1) for the first taxable year to which the election applies shall be the largest dollar amount of returned merchandise which would have been taken into account under this section for any of the 3 immediately preceding taxable years if this section had applied to such preceding 3 taxable years. This paragraph and paragraph (3) shall be applied by taking into account only amounts attributable to the trade or business for which such account is established.

(3) Adjustments in suspense account

At the close of each taxable year the suspense account shall be—

(A) reduced the excess (if any) of—

(i) the opening balance of the suspense account for the taxable year, over

(ii) the amount excluded from gross income for the taxable year under subsection (a), or

(B) increased (but not in excess of the initial opening balance) by the excess (if any) of—

(i) the amount excluded from gross income for the taxable year under subsection (a), over

(ii) the opening balance of the account for the taxable year.

(4) Gross income adjustments

(A) Reductions excluded from gross income

In the case of any reduction under paragraph (3)(A) in the account for the taxable year, an amount equal to such reduction shall be excluded from gross income for such taxable year.

(B) Increases added to gross income

In the case of any increase under paragraph (3)(B) in the account for the taxable year, an amount equal to such increase shall be included in gross income for such taxable year.

If the initial opening balance exceeds the dollar amount of returned merchandise which would have been taken into account under subsection (a) for the taxable year preceding the first taxable year for which the election is effective if this section had applied to such preceding taxable year, then an amount equal to the amount of such excess shall be included in gross income for such first taxable year.

(5) Subchapter C transactions

The application of this subsection with respect to a taxpayer which is a party to any transaction with respect to which there is nonrecognition of gain or loss to any party to the transaction by reason of subchapter C shall be determined under regulations prescribed by the Secretary.

(Added Pub. L. 95–600, title III, §372(a), Nov. 6, 1978, 92 Stat. 2860; amended Pub. L. 115–141, div. U, title IV, §401(a)(114), (115), Mar. 23, 2018, 132 Stat. 1189.)

AMENDMENTS

2018—Subsec. (b)(9). Pub. L. 115–141, §401(a)(114), substituted ''Repurchase'' for ''Repurchased'' in heading.

Subsec. (c)(1). Pub. L. 115–141, §401(a)(115), substituted ''regulations prescribe'' for ''regulations prescribed''.

EFFECTIVE DATE

Pub. L. 95–600, title III, §372(c), Nov. 6, 1978, 92 Stat. 2862, provided that: ''The amendments made by this section [enacting this section] shall apply to taxable years beginning after September 30, 1979.''

§ 460. Special rules for long-term contracts

(a) Requirement that percentage of completion method be used

In the case of any long-term contract, the taxable income from such contract shall be determined under the percentage of completion method (as modified by subsection (b)).

(b) Percentage of completion method

(1) Requirements of percentage of completion method

Except as provided in paragraph (3), in the case of any long-term contract with respect to which the percentage of completion method is used—

(A) the percentage of completion shall be determined by comparing costs allocated to the contract under subsection (c) and incurred before the close of the taxable year with the estimated total contract costs, and

(B) upon completion of the contract (or, with respect to any amount properly taken into account after completion of the contract, when such amount is so properly taken into account), the taxpayer shall pay (or shall be entitled to receive) interest computed under the look-back method of paragraph (2).

In the case of any long-term contract with respect to which the percentage of completion method is used, except for purposes of applying the look-back method of paragraph (2), any income under the contract (to the extent not previously includible in gross income) shall be included in gross income for the taxable year following the taxable year in which the contract was completed. For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under subparagraph (B) shall be treated as an increase in the tax imposed by this chapter for the taxable year in which the contract is completed (or, in the case of interest payable with respect to any amount properly taken into account after completion of the contract, for the taxable year in which the amount is so properly taken into account).

(2) Look-back method

The interest computed under the look-back method of this paragraph shall be determined by—

(A) first, allocating income under the contract among taxable years before the year in which the contract is completed on the basis of the actual contract price and costs instead of the estimated contract price and costs,

(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each taxable year referred to in subparagraph (A) which would result solely from the application of subparagraph (A), and

(C) then using the adjusted overpayment rate (as defined in paragraph (7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any amount properly taken into account after completion of the contract shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such amount was properly taken into account) such amount to its value as of the completion of the contract. The taxpayer may elect with respect to any contract to have the preceding sentence not apply to such contract.

(3) Special rules

(A) Simplified method of cost allocation

In the case of any long-term contract, the Secretary may prescribe a simplified procedure for allocation of costs to such contract in lieu of the method of allocation under subsection (c).

(B) Look-back method not to apply to certain contracts

Paragraph (1)(B) shall not apply to any contract—

(i) the gross price of which (as of the completion of the contract) does not exceed the lesser of—

(I) $1,000,000, or

(II) 1 percent of the average annual gross receipts of the taxpayer for the 3 taxable years preceding the taxable year in which the contract was completed, and

(ii) which is completed within 2 years of the contract commencement date.

For purposes of this subparagraph, rules similar to the rules of subsections (e)(2) and (f)(3) shall apply.

(4) Simplified look-back method for pass-thru entities

(A) In general

In the case of a pass-thru entity—

(i) the look-back method of paragraph (2) shall be applied at the entity level,

(ii) in determining overpayments and underpayments for purposes of applying paragraph (2)(B)—

(I) any increase in the income under the contract for any taxable year by reason of the allocation under paragraph (2)(A) shall be treated as giving rise to an underpayment determined by applying the highest rate for such year to such increase, and

(II) any decrease in such income for any taxable year by reason of such allocation shall be treated as giving rise to an overpayment determined by applying the highest rate for such year to such decrease, and

(iii) any interest required to be paid by the taxpayer under paragraph (2) shall be paid by such entity (and any interest entitled to be received by the taxpayer under paragraph (2) shall be paid to such entity).

(B) Exceptions

(i) Closely held pass-thru entities

This paragraph shall not apply to any closely held pass-thru entity.

(ii) Foreign contracts

This paragraph shall not apply to any contract unless substantially all of the in-

come from such contract is from sources in the United States.

(C) Other definitions

For purposes of this paragraph—

(i) Highest rate

The term ''highest rate'' means—

(I) the highest rate of tax specified in section 11, or

(II) if at all times during the year involved more than 50 percent of the interests in the entity are held by individuals directly or through 1 or more other pass-thru entities, the highest rate of tax specified in section 1.

(ii) Pass-thru entity

The term ''pass-thru entity'' means any—

(I) partnership,

(II) S corporation, or

(III) trust.

(iii) Closely held pass-thru entity

The term ''closely held pass-thru entity'' means any pass-thru entity if, at any time during any taxable year for which there is income under the contract, 50 percent or more (by value) of the beneficial interests in such entity are held (directly or indirectly) by or for 5 or fewer persons. For purposes of the preceding sentence, rules similar to the constructive ownership rules of section 1563(e) shall apply.

(5) Election to use 10-percent method

(A) General rule

In the case of any long-term contract with respect to which an election under this paragraph is in effect, the 10-percent method shall apply in determining the taxable income from such contract.

(B) 10-percent method

For purposes of this paragraph—

(i) In general

The 10-percent method is the percentage of completion method, modified so that any item which would otherwise be taken into account in computing taxable income with respect to a contract for any taxable year before the 10-percent year is taken into account in the 10-percent year.

(ii) 10-percent year

The term ''10-percent year'' means the 1st taxable year as of the close of which at least 10 percent of the estimated total contract costs have been incurred.

(C) Election

An election under this paragraph shall apply to all long-term contracts of the taxpayer which are entered into during the taxable year in which the election is made or any subsequent taxable year.

(D) Coordination with other provisions

(i) Simplified method of cost allocation

This paragraph shall not apply to any taxpayer which uses a simplified procedure for allocation of costs under paragraph (3)(A).

(ii) Look-back method

The 10-percent method shall be taken into account for purposes of applying the look-back method of paragraph (2) to any taxpayer making an election under this paragraph.

(6) Election to have look-back method not apply in de minimis cases

(A) Amounts taken into account after completion of contract

Paragraph (1)(B) shall not apply with respect to any taxable year (beginning after the taxable year in which the contract is completed) if—

(i) the cumulative taxable income (or loss) under the contract as of the close of such taxable year, is within

(ii) 10 percent of the cumulative look-back taxable income (or loss) under the contract as of the close of the most recent taxable year to which paragraph (1)(B) applied (or would have applied but for subparagraph (B)).

(B) De minimis discrepancies

Paragraph (1)(B) shall not apply in any case to which it would otherwise apply if—

(i) the cumulative taxable income (or loss) under the contract as of the close of each prior contract year, is within

(ii) 10 percent of the cumulative look-back income (or loss) under the contract as of the close of such prior contract year.

(C) Definitions

For purposes of this paragraph—

(i) Contract year

The term ''contract year'' means any taxable year for which income is taken into account under the contract.

(ii) Look-back income or loss

The look-back income (or loss) is the amount which would be the taxable income (or loss) under the contract if the allocation method set forth in paragraph (2)(A) were used in determining taxable income.

(iii) Discounting not applicable

The amounts taken into account after the completion of the contract shall be determined without regard to any discounting under the 2nd sentence of paragraph (2).

(D) Contracts to which paragraph applies

This paragraph shall only apply if the taxpayer makes an election under this subparagraph. Unless revoked with the consent of the Secretary, such an election shall apply to all long-term contracts completed during the taxable year for which election is made or during any subsequent taxable year.

(7) Adjusted overpayment rate

(A) In general

The adjusted overpayment rate for any interest accrual period is the overpayment rate in effect under section 6621 for the calendar quarter in which such interest accrual period begins.

(B) Interest accrual period

For purposes of subparagraph (A), the term ''interest accrual period'' means the period—

(i) beginning on the day after the return due date for any taxable year of the taxpayer, and

(ii) ending on the return due date for the following taxable year.

For purposes of the preceding sentence, the term ''return due date'' means the date prescribed for filing the return of the tax imposed by this chapter (determined without regard to extensions).

(c) Allocation of costs to contract

(1) Direct and certain indirect costs

In the case of a long-term contract, all costs (including research and experimental costs) which directly benefit, or are incurred by reason of, the long-term contract activities of the taxpayer shall be allocated to such contract in the same manner as costs are allocated to extended period long-term contracts under section 451 and the regulations thereunder.

(2) Costs identified under cost-plus and certain Federal contracts

In the case of a cost-plus long-term contract or a Federal long-term contract, any cost not allocated to such contract under paragraph (1) shall be allocated to such contract if such cost is identified by the taxpayer (or a related person), pursuant to the contract or Federal, State, or local law or regulation, as being attributable to such contract.

(3) Allocation of production period interest to contract

(A) In general

Except as provided in subparagraphs (B) and (C), in the case of a long-term contract, interest costs shall be allocated to the contract in the same manner as interest costs are allocated to property produced by the taxpayer under section 263A(f).

(B) Production period

In applying section 263A(f) for purposes of subparagraph (A), the production period shall be the period—

(i) beginning on the later of—

(I) the contract commencement date, or

(II) in the case of a taxpayer who uses an accrual method with respect to long-term contracts, the date by which at least 5 percent of the total estimated costs (including design and planning costs) under the contract have been incurred, and

(ii) ending on the contract completion date.

(C) Application of de minimis rule

In applying section 263A(f) for purposes of subparagraph (A), paragraph (1)(B)(iii) of such section shall be applied on a contract-by-contract basis; except that, in the case of a taxpayer described in subparagraph (B)(i)(II) of this paragraph, paragraph (1)(B)(iii) of section 263A(f) shall be applied on a property-by-property basis.

(4) Certain costs not included

This subsection shall not apply to any—

(A) independent research and development expenses,

(B) expenses for unsuccessful bids and proposals, and

(C) marketing, selling, and advertising expenses.

(5) Independent research and development expenses

For purposes of paragraph (4), the term ''independent research and development expenses'' means any expenses incurred in the performance of research or development, except that such term shall not include—

(A) any expenses which are directly attributable to a long-term contract in existence when such expenses are incurred, or

(B) any expenses under an agreement to perform research or development.

(6) Special rule for allocation of bonus depreciation with respect to certain property

(A) In general

Solely for purposes of determining the percentage of completion under subsection (b)(1)(A), the cost of qualified property shall be taken into account as a cost allocated to the contract as if subsection (k) of section 168 had not been enacted.

(B) Qualified property

For purposes of this paragraph, the term ''qualified property'' means property described in section 168(k)(2) which—

(i) has a recovery period of 7 years or less, and

(ii) is placed in service before January 1, 2027 (January 1, 2028 in the case of property described in section 168(k)(2)(B)).

(d) Federal long-term contract

For purposes of this section—

(1) In general

The term ''Federal long-term contract'' means any long-term contract—

(A) to which the United States (or any agency or instrumentality thereof) is a party, or

(B) which is a subcontract under a contract described in subparagraph (A).

(2) Special rules for certain taxable entities

For purposes of paragraph (1), the rules of section 168(h)(2)(D) (relating to certain taxable entities not treated as instrumentalities) shall apply.

(e) Exception for certain construction contracts

(1) In general

Subsections (a), (b), and (c)(1) and (2) shall not apply to—

(A) any home construction contract, or

(B) any other construction contract entered into by a taxpayer (other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under section 448(a)(3))—

(i) who estimates (at the time such contract is entered into) that such contract

will be completed within the 2-year period beginning on the contract commencement date of such contract, and

(ii) who meets the gross receipts test of section 448(c) for the taxable year in which such contract is entered into.

In the case of a home construction contract with respect to which the requirements of clauses (i) and (ii) of subparagraph (B) are not met, section 263A shall apply notwithstanding subsection (c)(4) thereof.

(2) Rules related to gross receipts test

(A) Application of gross receipts test to individuals, etc.

For purposes of paragraph (1)(B)(ii), in the case of any taxpayer which is not a corporation or a partnership, the gross receipts test of section 448(c) shall be applied in the same manner as if each trade or business of such taxpayer were a corporation or partnership.

(B) Coordination with section 481

Any change in method of accounting made pursuant to paragraph (1)(B)(ii) shall be treated as initiated by the taxpayer and made with the consent of the Secretary. Such change shall be effected on a cut-off basis for all similarly classified contracts entered into on or after the year of change.

(3) Construction contract

For purposes of this subsection, the term ''construction contract'' means any contract for the building, construction, reconstruction, or rehabilitation of, or the installation of any integral component to, or improvements of, real property.

(4) Special rule for residential construction contracts which are not home construction contracts

In the case of any residential construction contract which is not a home construction contract, subsection (a) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1989) shall apply except that such subsection shall be applied—

(A) by substituting ''70 percent'' for ''90 percent'' each place it appears, and

(B) by substituting ''30 percent'' for ''10 percent''.

(5) Definitions relating to residential construction contracts

For purposes of this subsection—

(A) Home construction contract

The term ''home construction contract'' means any construction contract if 80 percent or more of the estimated total contract costs (as of the close of the taxable year in which the contract was entered into) are reasonably expected to be attributable to activities referred to in paragraph (4) with respect to—

(i) dwelling units (as defined in section 168(e)(2)(A)(ii)) contained in buildings containing 4 or fewer dwelling units (as so defined), and

(ii) improvements to real property directly related to such dwelling units and located on the site of such dwelling units.

For purposes of clause (i), each townhouse or rowhouse shall be treated as a separate building.

(B) Residential construction contract

The term ''residential construction contract'' means any contract which would be described in subparagraph (A) if clause (i) of such subparagraph reads as follows:

''(i) dwelling units (as defined in section 168(e)(2)(A)(ii)), and''.

(f) Long-term contract

For purposes of this section—

(1) In general

The term ''long-term contract'' means any contract for the manufacture, building, installation, or construction of property if such contract is not completed within the taxable year in which such contract is entered into.

(2) Special rule for manufacturing contracts

A contract for the manufacture of property shall not be treated as a long-term contract unless such contract involves the manufacture of—

(A) any unique item of a type which is not normally included in the finished goods inventory of the taxpayer, or

(B) any item which normally requires more than 12 calendar months to complete (without regard to the period of the contract).

(3) Aggregation, etc.

For purposes of this subsection, under regulations prescribed by the Secretary—

(A) 2 or more contracts which are interdependent (by reason of pricing or otherwise) may be treated as 1 contract, and

(B) a contract which is properly treated as an aggregation of separate contracts may be so treated.

(g) Contract commencement date

For purposes of this section, the term ''contract commencement date'' means, with respect to any contract, the first date on which any costs (other than bidding expenses or expenses incurred in connection with negotiating the contract) allocable to such contract are incurred.

(h) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations to prevent the use of related parties, pass-thru entities, intermediaries, options, or other similar arrangements to avoid the application of this section.

(Added Pub. L. 99–514, title VIII, §804(a), Oct. 22, 1986, 100 Stat. 2358; amended Pub. L. 100–203, title X, §10203(a), Dec. 22, 1987, 101 Stat. 1330–394; Pub. L. 100–647, title I, §1008(c)(1), (2), (4), title V, §5041(a)–(b)(3), (c), (d), Nov. 10, 1988, 102 Stat. 3438, 3439, 3673, 3674; Pub. L. 101–239, title VII, §§7621(a)–(c), 7811(e), 7815(e)(1), Dec. 19, 1989, 103 Stat. 2375, 2376, 2408, 2419; Pub. L. 101–508, title XI, §11812(b)(8), Nov. 5, 1990, 104 Stat. 1388–535; Pub. L. 104–188, title I, §§1702(h)(15), 1704(t)(28), Aug. 20, 1996, 110 Stat. 1874, 1888; Pub. L. 105–34, title XII, §1211(a), (b), Aug. 5, 1997, 111 Stat. 998,

999; Pub. L. 111–240, title II, §2023(a), Sept. 27, 2010, 124 Stat. 2559; Pub. L. 112–240, title III, §331(b), Jan. 2, 2013, 126 Stat. 2336; Pub. L. 113–295, div. A, title I, §125(b), Dec. 19, 2014, 128 Stat. 4016; Pub. L. 114–113, div. Q, title I, §143(a)(2), (b)(6)(I), Dec. 18, 2015, 129 Stat. 3056, 3064; Pub. L. 115–97, title I, §§13102(d), 13201(b)(2)(A), Dec. 22, 2017, 131 Stat. 2104, 2107; Pub. L. 115–141, div. U, title IV, §401(a)(116), Mar. 23, 2018, 132 Stat. 1189.)

REFERENCES IN TEXT

The date of the enactment of the Revenue Reconciliation Act of 1989, referred to in subsec. (e)(4), is the date of enactment of title VII of Pub. L. 101–239, which was approved Dec. 19, 1989.

AMENDMENTS

2018—Subsec. (b)(2)(A). Pub. L. 115–141 inserted comma after ''first''.

2017—Subsec. (c)(6)(B)(ii). Pub. L. 115–97, §13201(b)(2)(A), substituted ''January 1, 2027 (January 1, 2028'' for ''January 1, 2020 (January 1, 2021''.

Subsec. (e)(1)(B). Pub. L. 115–97, §13102(d)(1)(A), in introductory provisions, inserted ''(other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under section 448(a)(3))'' after ''taxpayer''.

Subsec. (e)(1)(B)(ii). Pub. L. 115–97, §13102(d)(1)(B), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: ''whose average annual gross receipts for the 3 taxable years preceding the taxable year in which such contract is entered into do not exceed $10,000,000.''

Subsec. (e)(2). Pub. L. 115–97, §13102(d)(2), added par. (2) and struck out former par. (2) which related to determination of taxpayer's gross receipts.

Subsec. (e)(3) to (6). Pub. L. 115–97, §13102(d)(2), redesignated pars. (4) to (6) as (3) to (5), respectively, and struck out former par. (3) which related to controlled group of corporations.

2015—Subsec. (c)(6)(B)(ii). Pub. L. 114–113, §143(b)(6)(I), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: ''is placed in service after December 31, 2009, and before January 1, 2011 (January 1, 2012, in the case of property described in section 168(k)(2)(B)), or after December 31, 2012, and before January 1, 2016 (January 1, 2017, in the case of property described in section 168(k)(2)(B)).''

Subsec. (c)(6)(B)(ii). Pub. L. 114–113, §143(a)(2), substituted ''January 1, 2016 (January 1, 2017'' for ''January 1, 2015 (January 1, 2016''.

2014—Subsec. (c)(6)(B)(ii). Pub. L. 113–295 substituted ''January 1, 2015 (January 1, 2016'' for ''January 1, 2014 (January 1, 2015''.

2013—Subsec. (c)(6)(B)(ii). Pub. L. 112–240 inserted '', or after December 31, 2012, and before January 1, 2014 (January 1, 2015, in the case of property described in section 168(k)(2)(B))'' before period at end.

2010—Subsec. (c)(6). Pub. L. 111–240 added par. (6).

1997—Subsec. (b)(2)(C). Pub. L. 105–34, §1211(b)(1), substituted ''the adjusted overpayment rate (as defined in paragraph (7))'' for ''the overpayment rate established by section 6621''.

Subsec. (b)(6). Pub. L. 105–34, §1211(a), added par. (6).

Subsec. (b)(7). Pub. L. 105–34, §1211(b)(2), added par. (7).

1996—Subsec. (b)(1). Pub. L. 104–188, §1704(t)(28), which directed that par. (1) be amended by substituting ''the look-back method of paragraph (2)'' for ''the look-back method of paragraph (3)'', could not be executed, because that phrase does not appear in text. See 1989 Amendment note below.

Subsec. (e)(6)(B). Pub. L. 104–188, §1702(h)(15), substituted ''section 168(e)(2)(A)(ii)'' for ''section 167(k)''.

1990—Subsec. (e)(6)(A)(i). Pub. L. 101–508 substituted ''section 168(e)(2)(A)(ii)'' for ''section 167(k)''.

1989—Subsec. (a). Pub. L. 101–239, §7621(a), substituted ''Requirement that percentage of completion method be used'' for ''Percentage of completion-capitalized cost method'' in heading and amended text generally. Prior to amendment, text read as follows:

''(1) IN GENERAL.—In the case of any long-term contract—

''(A) 90 percent of the items with respect to such contract shall be taken into account under the percentage of completion method (as modified by subsection (b)), and

''(B) 10 percent of the items with respect to such contract shall be taken into account under the taxpayer's normal method of accounting.

''(2) 90 PERCENT LOOK-BACK METHOD TO APPLY.—Upon completion of any long-term contract (or, with respect to any amount properly taken into account after completion of the contract, when such amount is so properly taken into account), the taxpayer shall pay (or shall be entitled to receive) interest determined by applying the look-back method of subsection (b)(3) to 90 percent of the items with respect to the contract.''

Subsec. (a)(2). Pub. L. 101–239, §7811(e)(1), inserted ''(or, with respect to any amount properly taken into account after completion of the contract, when such amount is so properly taken into account)'' after ''any long-term contract''.

Subsec. (b)(1). Pub. L. 101–239, §7621(c)(2)(A), substituted ''paragraph (3)'' for ''paragraph (4)''.

Pub. L. 101–239, §7621(c)(2)(B), which directed the amendment of par. (1) by substituting ''paragraph (2)'' for ''paragraph (3)'', was executed by making the substitution in subpar. (B) and concluding provisions to reflect the probable intent of Congress.

Pub. L. 101–239, §7621(c)(1), redesignated par. (2) as (1) and struck out former par. (1) which read as follows: ''SUBSECTION (a) NOT TO APPLY WHERE PERCENTAGE OF COMPLETION METHOD USED.—Subsection (a) shall not apply to any long-term contract with respect to which amounts includible in gross income are determined under the percentage of completion method.''

Subsec. (b)(2). Pub. L. 101–239, §7621(c)(1), redesignated par. (3) as (2). Former par. (2) redesignated (1).

Pub. L. 101–239, §7811(e)(4), (6), inserted two sentences at end.

Subsec. (b)(2)(B). Pub. L. 101–239, §7811(e)(2), substituted ''any amount properly taken into account'' for ''any amount received or accrued'' and ''is so properly taken into account'' for ''is so received or accrued''.

Subsec. (b)(3). Pub. L. 101–239, §7621(c)(1), redesignated par. (4) as (3). Former par. (3) redesignated (2).

Pub. L. 101–239, §7811(e)(3), in concluding provisions, substituted ''any amount properly taken into account'' for ''any amount received or accrued'' and ''such amount was properly taken into account'' for ''such amount was received or accrued''.

Subsec. (b)(3)(B). Pub. L. 101–239, §7621(c)(3), substituted ''Paragraph (1)(B)'' for ''Paragraph (2)(B) and subsection (a)(2)'' in introductory provisions.

Subsec. (b)(4). Pub. L. 101–239, §7621(c)(1), redesignated par. (5) as (4). Former par. (4) redesignated (3).

Subsec. (b)(4)(A)(i). Pub. L. 101–239, §7621(c)(4)(A), substituted ''paragraph (2)'' for ''paragraph (3)''.

Subsec. (b)(4)(A)(ii). Pub. L. 101–239, §7621(c)(4)(B), substituted ''paragraph (2)(B)'' for ''paragraph (3)(B)'' in introductory provisions.

Subsec. (b)(4)(A)(ii)(I). Pub. L. 101–239, §7621(c)(4)(C), substituted ''paragraph (2)(A)'' for ''paragraph (3)(A)''.

Subsec. (b)(4)(A)(iii). Pub. L. 101–239, §7621(c)(4)(A), substituted ''paragraph (2)'' for ''paragraph (3)'' in two places.

Subsec. (b)(5). Pub. L. 101–239, §7621(b), added par. (5).

Pub. L. 101–239, §7621(c)(1), redesignated former par. (5) as (4).

Subsec. (e)(2)(C). Pub. L. 101–239, §7811(e)(5), added subpar. (C).

Subsec. (e)(5). Pub. L. 101–239, §7621(c)(5), inserted introductory provisions and struck out former introductory provisions which read as follows: ''In the case of any residential construction contract which is not a home construction contract, subsection (a) shall be applied—''.

Subsec. (e)(6)(A). Pub. L. 101–239, §7815(e)(1)(A), substituted ''activities referred to in paragraph (4) with respect to'' for ''the building, construction, reconstruction, or rehabilitation of''.

Subsec. (e)(6)(A)(i). Pub. L. 101–239, §7815(e)(1)(B), added cl. (i) and struck out former cl. (i) which read as follows: ''dwelling units contained in buildings containing 4 or fewer dwelling units, and''.

1988—Subsec. (a)(1)(A). Pub. L. 100–647, §5041(a)(1), substituted ''90'' for ''70''.

Subsec. (a)(1)(B). Pub. L. 100–647, §5041(a)(2), substituted ''10'' for ''30''.

Subsec. (a)(2). Pub. L. 100–647, §5041(a)(1), substituted ''90'' for ''70'' in heading and in text.

Subsec. (b)(2). Pub. L. 100–647, §1008(c)(2)(B), substituted ''Except as provided in paragraph (4), in'' for ''In''.

Subsec. (b)(2)(B). Pub. L. 100–647, §1008(c)(4)(B), inserted ''(or, with respect to any amount received or accrued after completion of the contract, when such amount is so received or accrued)'' after ''contract''.

Subsec. (b)(3). Pub. L. 100–647, §1008(c)(4)(A), inserted at end ''For purposes of the preceding sentence, any amount received or accrued after completion of the contract shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such amount was received or accrued) such amount to its value as of the completion of the contract. The taxpayer may elect with respect to any contract to have the preceding sentence not apply to such contract.''

Pub. L. 100–647, §1008(c)(1)(A), substituted ''paragraph'' for ''subparagraph''.

Subsec. (b)(3)(B). Pub. L. 100–647, §1008(c)(1)(B), substituted ''subparagraph (A)'' for ''paragraph (1)'' in two places.

Subsec. (b)(3)(C). Pub. L. 100–647, §1008(c)(1)(C), substituted ''subparagraph (B)'' for ''paragraph (1)''.

Subsec. (b)(4). Pub. L. 100–647, §1008(c)(2)(A), added par. (4).

Subsec. (b)(5). Pub. L. 100–647, §5041(d), added par. (5).

Subsec. (e)(1). Pub. L. 100–647, §5041(b)(1), amended par. (1) generally. Prior to amendment, par. (1) read as follows: ''Subsections (a), (b), and (c)(1) and (2) shall not apply to any construction contract entered into by a taxpayer—

''(A) who estimates (at the time such contract is entered into) that such contract will be completed within the 2-year period beginning on the contract commencement date of such contract, and

''(B) whose average annual gross receipts for the 3 taxable years preceding the taxable year in which such contract is entered into do not exceed $10,000,000.''

Subsec. (e)(5). Pub. L. 100–647, §5041(b)(2), added par. (5).

Subsec. (e)(6). Pub. L. 100–647, §5041(b)(3), added par. (6).

Subsec. (h). Pub. L. 100–647, §5041(c), added subsec. (h).

1987—Subsec. (a). Pub. L. 100–203 substituted ''70 percent'' for ''40 percent'' in par. (1)(A) and in heading and text of par. (2), and ''30 percent'' for ''60 percent'' in par. (1)(B).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by section 13102(d) of Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, with provision for exemption from percentage completion for long-term contracts, see section 13102(e) of Pub. L. 115–97, set out as a note under section 263A of this title.

Amendment by section 13201 of Pub. L. 115–97 applicable to property acquired and placed in service after Sept. 27, 2017, and specified plants planted or grafted after Sept. 27, 2017, see section 13201(h) of Pub. L. 115–97, set out as a note under section 168 of this title.

EFFECTIVE DATE OF 2015 AMENDMENT

Amendment by section 143(a)(2) of Pub. L. 114–113 applicable to property placed in service after Dec. 31, 2014, in taxable years ending after such date, see section 143(a)(5) of Pub. L. 114–113, set out as a note under section 168 of this title.

Amendment by section 143(b)(6)(I) of Pub. L. 114–113 applicable to property placed in service after Dec. 31, 2015, in taxable years ending after such date, see section 143(b)(7) of Pub. L. 114–113, set out as a note under section 168 of this title.

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 applicable to property placed in service after Dec. 31, 2013, in taxable years ending after such date, see section 125(e) of Pub. L. 113–295, set out as a note under section 168 of this title.

EFFECTIVE DATE OF 2013 AMENDMENT

Amendment by Pub. L. 112–240 applicable to property placed in service after Dec. 31, 2012, in taxable years ending after such date, see section 331(f) of Pub. L. 112–240, set out as a note under section 168 of this title.

EFFECTIVE DATE OF 2010 AMENDMENT

Pub. L. 111–240, title II, §2023(b), Sept. 27, 2010, 124 Stat. 2559, provided that: ''The amendment made by this section [amending this section] shall apply to property placed in service after December 31, 2009.''

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105–34, title XII, §1211(c), Aug. 5, 1997, 111 Stat. 1000, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to contracts completed in taxable years ending after the date of the enactment of this Act [Aug. 5, 1997].

''(2) SUBSECTION (b).—The amendments made by subsection (b) [amending this section] shall apply for purposes of section 167(g) of the Internal Revenue Code of 1986 to property placed in service after September 13, 1995.''

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by section 1702(h)(15) of Pub. L. 104–188 effective, except as otherwise expressly provided, as if included in the provision of the Revenue Reconciliation Act of 1990, Pub. L. 101–508, title XI, to which such amendment relates, see section 1702(i) of Pub. L. 104–188, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101–508 applicable to property placed in service after Nov. 5, 1990, but not applicable to any property to which section 168 of this title does not apply by reason of subsec. (f)(5) of section 168, and not applicable to rehabilitation expenditures described in section 252(f)(5) of Pub. L. 99–514, see section 11812(c) of Pub. L. 101–508, set out as a note under section 42 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Pub. L. 101–239, title VII, §7621(d), Dec. 19, 1989, 103 Stat. 2376, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to contracts entered into on or after July 11, 1989.

''(2) BINDING BIDS.—The amendments made by this section shall not apply to any contract resulting from the acceptance of a bid made before July 11, 1989. The preceding sentence shall apply only if the bid could not have been revoked or altered at any time on or after July 11, 1989.

''(3) SPECIAL RULE FOR CERTAIN SHIP CONTRACTS.—The amendments made by this section shall not apply in the case of a qualified ship contract (as defined in section 10203(b)(2)(B) of the Revenue Act of 1987 [Pub. L. 100–203, set out below]).''

Amendment by sections 7811(e) and 7815(e)(1) of Pub. L. 101–239 effective, except as otherwise provided, as if

included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 7817 of Pub. L. 101–239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1008(c)(1), (2), (4) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Pub. L. 100–647, title V, § 5041(e), Nov. 10, 1988, 102 Stat. 3675, as amended by Pub. L. 101–239, title VII, § 7815(e)(3), Dec. 19, 1989, 103 Stat. 2419, provided that:

''(1) SUBSECTIONS (a), (b), AND (c).—

''(A) IN GENERAL.—Except as otherwise provided in this paragraph, the amendments made by subsections (a), (b), and (c) [amending this section and section 56 of this title] shall apply to contracts entered into on or after June 21, 1988.

''(B) BINDING BIDS.—The amendments made by subsections (a), (b), and (c) shall not apply to any contract resulting from the acceptance of a bid made before June 21, 1988. The preceding sentence shall apply only if the bid could not have been revoked or altered at any time on or after June 21, 1988.

''(C) SPECIAL RULE FOR CERTAIN SHIP CONTRACTS.—The amendments made by subsections (a) and (b) [amending this section and section 56 of this title] shall not apply in the case of a qualified ship contract (as defined in section 10203(b)(2)(B) of the Revenue Act of 1987 [Pub. L. 100–203, set out below]).

''(2) SUBSECTION (d).—The amendment made by subsection (d) [amending this section] shall apply as if included in the amendments made by section 804 of the Reform Act [Pub. L. 99–514]; except that such amendment shall not apply to any contract completed in a taxable year ending before the date of the enactment of this Act [Nov. 10, 1988], if the due date (determined with regard to extensions) for the return for such year is before such date of enactment.''

EFFECTIVE DATE OF 1987 AMENDMENT

Pub. L. 100–203, title X, § 10203(b), Dec. 22, 1987, 101 Stat. 1330–394, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to contracts entered into after October 13, 1987.

''(2) SPECIAL RULE FOR CERTAIN SHIP CONTRACTS.—

''(A) IN GENERAL.—The amendments made by this section shall not apply in the case of a qualified ship contract.

''(B) QUALIFIED SHIP CONTRACT.—For purposes of subparagraph (A), the term 'qualified ship contract' means any contract for the construction in the United States of not more than 5 ships if—

''(i) such ships will not be constructed (directly or indirectly) for the Federal Government, and

''(ii) the taxpayer reasonably expects to complete such contract within 5 years of the contract commencement date (as defined in section 460(g) of the Internal Revenue Code of 1986).''

EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99–514, title VIII, § 804(d), Oct. 22, 1986, 100 Stat. 2361, as amended by Pub. L. 100–647, title I, § 1008(c)(3), Nov. 10, 1988, 102 Stat. 3439, provided that:

''(1) IN GENERAL.—The amendments made by this section [enacting this section] shall apply to any contract entered into after February 28, 1986.

''(2) CLARIFICATION OF TREATMENT OF INDEPENDENT RESEARCH AND DEVELOPMENT EXPENSES.—

''(A) IN GENERAL.—For periods before, on, or after the date of enactment of this Act [Oct. 22, 1986]—

''(i) any independent research and development expenses taken into account in determining the total contract price shall not be severable from the contract, and

''(ii) any independent research and development expenses shall not be treated as amounts chargeable to capital account.

''(B) INDEPENDENT RESEARCH AND DEVELOPMENT EXPENSES.—For purposes of subparagraph (A), the term 'independent research and development expenses' has the meaning given to such term by section 460(c)(5) of the Internal Revenue Code of 1986, as added by this section.''

REGULATIONS

Pub. L. 99–514, title VIII, § 804(b), Oct. 22, 1986, 100 Stat. 2361, provided that: ''The Secretary of the Treasury or his delegate shall modify the income tax regulations relating to accounting for long-term contracts to carry out the provisions of section 460 of the Internal Revenue Code of 1986 (as added by subsection (a)).''

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

METHOD OF ACCOUNTING FOR NAVAL SHIPBUILDERS

Pub. L. 108–357, title VII, § 708, Oct. 22, 2004, 118 Stat. 1550, as amended by Pub. L. 109–135, title IV, § 403(s), Dec. 21, 2005, 119 Stat. 2628, provided that:

''(a) IN GENERAL.—In the case of a qualified naval ship contract, the taxable income of such contract during the 5-taxable year period beginning with the taxable year in which the construction commencement date occurs shall be determined under a method identical to the method used in the case of a qualified ship contract (as defined in section 10203(b)(2)(B) of the Revenue Act of 1987 [Pub. L. 100–203, set out as an Effective Date of 1987 Amendment note above]).

''(b) RECAPTURE OF TAX BENEFIT.—In the case of a qualified naval ship contract to which subsection (a) applies, the taxpayer's tax imposed by chapter 1 of the Internal Revenue Code of 1986 for the first taxable year following the 5-taxable year period described in subsection (a) shall be increased by the excess (if any) of—

''(1) the amount of tax which would have been imposed during such period if this section had not been enacted, over

''(2) the amount of tax so imposed during such period.

''(c) QUALIFIED NAVAL SHIP CONTRACT.—For purposes of this section:

''(1) IN GENERAL.—The term 'qualified naval ship contract' means any contract or portion thereof that is for the construction in the United States of 1 ship or submarine for the Federal Government if the taxpayer reasonably expects the acceptance date will occur no later than 9 years after the construction commencement date.

''(2) ACCEPTANCE DATE.—The term 'acceptance date' means the date 1 year after the date on which the Federal Government issues a letter of acceptance or other similar document for the ship or submarine.

''(3) CONSTRUCTION COMMENCEMENT DATE.—The term 'construction commencement date' means the date on which the physical fabrication of any section or component of the ship or submarine begins in the taxpayer's shipyard.

''(d) CERTAIN ADJUSTMENTS NOT TO APPLY.—Section 481 of the Internal Revenue Code of 1986 shall not apply with respect to any change in the method of accounting which is required by this section.

''(e) EFFECTIVE DATE.—This section shall apply to contracts for ships or submarines with respect to which the construction commencement date occurs after the date of the enactment of this Act [Oct. 22, 2004].''

AMORTIZATION OF PAST SERVICE PENSION COSTS

Allocable costs (within the meaning of subsec. (c) of this section) with respect to any property to include

contributions paid to or under a pension or annuity plan whether or not such contributions represent past service costs, see section 10204 of Pub. L. 100–203, set out as a note under section 263A of this title.

SUBPART C—TAXABLE YEAR FOR WHICH DEDUCTIONS TAKEN

AMENDMENTS

2004—Pub. L. 108–357, title VIII, §848(b), Oct. 22, 2004, 118 Stat. 1606, added item 470.

1987—Pub. L. 100–203, title X, §10201(b)(7), Dec. 22, 1987, 101 Stat. 1330–387, struck out item 463 ''Accrual of vacation pay''.

1986—Pub. L. 99–514, title IV, §404(b)(2), title V, §501(b), title VIII, §823(b)(2), title XVIII, §§1807(a)(7)(B), 1899A(71), Oct. 22, 1986, 100 Stat. 2224, 2241, 2374, 2815, 2963, substituted ''for certain farming expenses'' for ''in case of farming syndicates'' in item 464, struck out item 466 ''Qualified discount coupons redeemed after close of taxable year'', inserted ''the'' before ''use'' in item 467, and added items 468B and 469.

1984—Pub. L. 98–369, div. A, title I, §§91(b)(2), (c)(2), 92(b), July 18, 1984, 98 Stat. 604, 606, 612, added items 467, 468, and 468A.

1978—Pub. L. 95–600, title II, §201(c)(2), title III, §373(b), Nov. 6, 1978, 92 Stat. 2816, 2865, struck out ''in case of certain activities'' after ''amount at risk'' in item 465 and added item 466.

1976—Pub. L. 94–455, title II, §§204(b), 207(a)(2), Oct. 4, 1976, 90 Stat. 1532, 1537, added items 464 and 465.

1975—Pub. L. 93–625, §4(b), Jan. 3, 1975, 88 Stat. 2111, added item 463.

1955—Act June 15, 1955, ch. 143, §2(3), 69 Stat. 135, struck out item 462 ''Reserves for estimated expenses, etc.''

§461. General rule for taxable year of deduction

(a) General rule

The amount of any deduction or credit allowed by this subtitle shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income.

(b) Special rule in case of death

In the case of the death of a taxpayer whose taxable income is computed under an accrual method of accounting, any amount accrued as a deduction or credit only by reason of the death of the taxpayer shall not be allowed in computing taxable income for the period in which falls the date of the taxpayer's death.

(c) Accrual of real property taxes

(1) In general

If the taxable income is computed under an accrual method of accounting, then, at the election of the taxpayer, any real property tax which is related to a definite period of time shall be accrued ratably over that period.

(2) When election may be made

(A) Without consent

A taxpayer may, without the consent of the Secretary, make an election under this subsection for his first taxable year in which he incurs real property taxes. Such an election shall be made not later than the time prescribed by law for filing the return for such year (including extensions thereof).

(B) With consent

A taxpayer may, with the consent of the Secretary, make an election under this subsection at any time.

(d) Limitation on acceleration of accrual of taxes

(1) General rule

In the case of a taxpayer whose taxable income is computed under an accrual method of accounting, to the extent that the time for accruing taxes is earlier than it would be but for any action of any taxing jurisdiction taken after December 31, 1960, then, under regulations prescribed by the Secretary, such taxes shall be treated as accruing at the time they would have accrued but for such action by such taxing jurisdiction.

(2) Limitation

Under regulations prescribed by the Secretary, paragraph (1) shall be inapplicable to any item of tax to the extent that its application would (but for this paragraph) prevent all persons (including successors in interest) from ever taking such item into account.

(e) Dividends or interest paid on certain deposits or withdrawable accounts

Except as provided in regulations prescribed by the Secretary, amounts paid to, or credited to the accounts of, depositors or holders of accounts as dividends or interest on their deposits or withdrawable accounts (if such amounts paid or credited are withdrawable on demand subject only to customary notice to withdraw) by a mutual savings bank not having capital stock represented by shares, a domestic building and loan association, or a cooperative bank shall not be allowed as a deduction for the taxable year to the extent such amounts are paid or credited for periods representing more than 12 months. Any such amount not allowed as a deduction as the result of the application of the preceding sentence shall be allowed as a deduction for such other taxable year as the Secretary determines to be consistent with the preceding sentence.

(f) Contested liabilities

If—

(1) the taxpayer contests an asserted liability,

(2) the taxpayer transfers money or other property to provide for the satisfaction of the asserted liability,

(3) the contest with respect to the asserted liability exists after the time of the transfer, and

(4) but for the fact that the asserted liability is contested, a deduction would be allowed for

the taxable year of the transfer (or for an earlier taxable year) determined after application of subsection (h),

then the deduction shall be allowed for the taxable year of the transfer. This subsection shall not apply in respect of the deduction for income, war profits, and excess profits taxes imposed by the authority of any foreign country or possession of the United States.

(g) Prepaid interest

(1) In general

If the taxable income of the taxpayer is computed under the cash receipts and disbursements method of accounting, interest paid by the taxpayer which, under regulations prescribed by the Secretary, is properly allocable to any period—

(A) with respect to which the interest represents a charge for the use or forbearance of money, and

(B) which is after the close of the taxable year in which paid,

shall be charged to capital account and shall be treated as paid in the period to which so allocable.

(2) Exception

This subsection shall not apply to points paid in respect of any indebtedness incurred in connection with the purchase or improvement of, and secured by, the principal residence of the taxpayer to the extent that, under regulations prescribed by the Secretary, such payment of points is an established business practice in the area in which such indebtedness is incurred, and the amount of such payment does not exceed the amount generally charged in such area.

(h) Certain liabilities not incurred before economic performance

(1) In general

For purposes of this title, in determining whether an amount has been incurred with respect to any item during any taxable year, the all events test shall not be treated as met any earlier than when economic performance with respect to such item occurs.

(2) Time when economic performance occurs

Except as provided in regulations prescribed by the Secretary, the time when economic performance occurs shall be determined under the following principles:

(A) Services and property provided to the taxpayer

If the liability of the taxpayer arises out of—

(i) the providing of services to the taxpayer by another person, economic performance occurs as such person provides such services,

(ii) the providing of property to the taxpayer by another person, economic performance occurs as the person provides such property, or

(iii) the use of property by the taxpayer, economic performance occurs as the taxpayer uses such property.

(B) Services and property provided by the taxpayer

If the liability of the taxpayer requires the taxpayer to provide property or services, economic performance occurs as the taxpayer provides such property or services.

(C) Workers compensation and tort liabilities of the taxpayer

If the liability of the taxpayer requires a payment to another person and—

(i) arises under any workers compensation act, or

(ii) arises out of any tort,

economic performance occurs as the payments to such person are made. Subparagraphs (A) and (B) shall not apply to any liability described in the preceding sentence.

(D) Other items

In the case of any other liability of the taxpayer, economic performance occurs at the time determined under regulations prescribed by the Secretary.

(3) Exception for certain recurring items

(A) In general

Notwithstanding paragraph (1) an item shall be treated as incurred during any taxable year if—

(i) the all events test with respect to such item is met during such taxable year (determined without regard to paragraph (1)),

(ii) economic performance with respect to such item occurs within the shorter of—

(I) a reasonable period after the close of such taxable year, or

(II) 8½ months after the close of such taxable year,

(iii) such item is recurring in nature and the taxpayer consistently treats items of such kind as incurred in the taxable year in which the requirements of clause (i) are met, and

(iv) either—

(I) such item is not a material item, or

(II) the accrual of such item in the taxable year in which the requirements of clause (i) are met results in a more proper match against income than accruing such item in the taxable year in which economic performance occurs.

(B) Financial statements considered under subparagraph (A)(iv)

In making a determination under subparagraph (A)(iv), the treatment of such item on financial statements shall be taken into account.

(C) Paragraph not to apply to workers compensation and tort liabilities

This paragraph shall not apply to any item described in subparagraph (C) of paragraph (2).

(4) All events test

For purposes of this subsection, the all events test is met with respect to any item if all events have occurred which determine the

fact of liability and the amount of such liability can be determined with reasonable accuracy.

(5) Subsection not to apply to certain items

This subsection shall not apply to any item for which a deduction is allowable under a provision of this title which specifically provides for a deduction for a reserve for estimated expenses.

(i) Special rules for tax shelters

(1) Recurring item exception not to apply

In the case of a tax shelter, economic performance shall be determined without regard to paragraph (3) of subsection (h).

(2) Special rule for spudding of oil or gas wells

(A) In general

In the case of a tax shelter, economic performance with respect to amounts paid during the taxable year for drilling an oil or gas well shall be treated as having occurred within a taxable year if drilling of the well commences before the close of the 90th day after the close of the taxable year.

(B) Deduction limited to cash basis

(i) Tax shelter partnerships

In the case of a tax shelter which is a partnership, in applying section 704(d) to a deduction or loss for any taxable year attributable to an item which is deductible by reason of subparagraph (A), the term ''cash basis'' shall be substituted for the term ''adjusted basis''.

(ii) Other tax shelters

Under regulations prescribed by the Secretary, in the case of a tax shelter other than a partnership, the aggregate amount of the deductions allowable by reason of subparagraph (A) for any taxable year shall be limited in a manner similar to the limitation under clause (i).

(C) Cash basis defined

For purposes of subparagraph (B), a partner's cash basis in a partnership shall be equal to the adjusted basis of such partner's interest in the partnership, determined without regard to—

(i) any liability of the partnership, and

(ii) any amount borrowed by the partner with respect to such partnership which—

(I) was arranged by the partnership or by any person who participated in the organization, sale, or management of the partnership (or any person related to such person within the meaning of section 465(b)(3)(C)), or

(II) was secured by any asset of the partnership.

(3) Tax shelter defined

For purposes of this subsection, the term ''tax shelter'' means—

(A) any enterprise (other than a C corporation) if at any time interests in such enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having the authority to regulate the offering of securities for sale,

(B) any syndicate (within the meaning of section 1256(e)(3)(B)), and

(C) any tax shelter (as defined in section 6662(d)(2)(C)(ii)).

(4) Special rules for farming

In the case of the trade or business of farming (as defined in section 464(e)), in determining whether an entity is a tax shelter, the definition of farming syndicate in subsection (k) shall be substituted for subparagraphs (A) and (B) of paragraph (3).

(5) Economic performance

For purposes of this subsection, the term ''economic performance'' has the meaning given such term by subsection (h).

(j) Limitation on excess farm losses of certain taxpayers

(1) Limitation

If a taxpayer other than a C corporation receives any applicable subsidy for any taxable year, any excess farm loss of the taxpayer for the taxable year shall not be allowed.

(2) Disallowed loss carried to next taxable year

Any loss which is disallowed under paragraph (1) shall be treated as a deduction of the taxpayer attributable to farming businesses in the next taxable year.

(3) Applicable subsidy

For purposes of this subsection, the term ''applicable subsidy'' means—

(A) any direct or counter-cyclical payment under title I of the Food, Conservation, and Energy Act of 2008, or any payment elected to be received in lieu of any such payment, or

(B) any Commodity Credit Corporation loan.

(4) Excess farm loss

For purposes of this subsection—

(A) In general

The term ''excess farm loss'' means the excess of—

(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to farming businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1)), over

(ii) the sum of—

(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such farming businesses, plus

(II) the threshold amount for the taxable year.

(B) Threshold amount

(i) In general

The term ''threshold amount'' means, with respect to any taxable year, the greater of—

(I) $300,000 ($150,000 in the case of married individuals filing separately), or

(II) the excess (if any) of the aggregate amounts described in subparagraph

(A)(ii)(I) for the 5-consecutive taxable year period preceding the taxable year over the aggregate amounts described in subparagraph (A)(i) for such period.

(ii) Special rules for determining aggregate amounts

For purposes of clause (i)(II)—

(I) notwithstanding the disregard in subparagraph (A)(i) of any disallowance under paragraph (1), in the case of any loss which is carried forward under paragraph (2) from any taxable year, such loss (or any portion thereof) shall be taken into account for the first taxable year in which a deduction for such loss (or portion) is not disallowed by reason of this subsection, and

(II) the Secretary shall prescribe rules for the computation of the aggregate amounts described in such clause in cases where the filing status of the taxpayer is not the same for the taxable year and each of the taxable years in the period described in such clause.

(C) Farming business

(i) In general

The term ''farming business'' has the meaning given such term in section 263A(e)(4).

(ii) Certain trades and businesses included

If, without regard to this clause, a taxpayer is engaged in a farming business with respect to any agricultural or horticultural commodity—

(I) the term ''farming business'' shall include any trade or business of the taxpayer of the processing of such commodity (without regard to whether the processing is incidental to the growing, raising, or harvesting of such commodity), and

(II) if the taxpayer is a member of a cooperative to which subchapter T applies, any trade or business of the cooperative described in subclause (I) shall be treated as the trade or business of the taxpayer.

(D) Certain losses disregarded

For purposes of subparagraph (A)(i), there shall not be taken into account any deduction for any loss arising by reason of fire, storm, or other casualty, or by reason of disease or drought, involving any farming business.

(5) Application of subsection in case of partnerships and S corporations

In the case of a partnership or S corporation—

(A) this subsection shall be applied at the partner or shareholder level, and

(B) each partner's or shareholder's proportionate share of the items of income, gain, or deduction of the partnership or S corporation for any taxable year from farming businesses attributable to the partnership or S corporation, and of any applicable subsidies received by the partnership or S corporation during the taxable year, shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

The Secretary may provide rules for the application of this paragraph to any other passthru entity to the extent necessary to carry out the provisions of this subsection.

(6) Additional reporting

The Secretary may prescribe such additional reporting requirements as the Secretary determines appropriate to carry out the purposes of this subsection.

(7) Coordination with section 469

This subsection shall be applied before the application of section 469.

(k) Farming syndicate defined

(1) In general

For purposes of subsection (i)(4), the term ''farming syndicate'' means—

(A) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if at any time interests in such partnership or enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having authority to regulate the offering of securities for sale, or

(B) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if more than 35 percent of the losses during any period are allocable to limited partners or limited entrepreneurs.

(2) Holdings attributable to active management

For purposes of paragraph (1)(B), the following shall be treated as an interest which is not held by a limited partner or a limited entrepreneur:

(A) in the case of any individual who has actively participated (for a period of not less than 5 years) in the management of any trade or business of farming, any interest in a partnership or other enterprise which is attributable to such active participation,

(B) in the case of any individual whose principal residence is on a farm, any partnership or other enterprise engaged in the trade or business of farming such farm,

(C) in the case of any individual who is actively participating in the management of any trade or business of farming or who is an individual who is described in subparagraph (A) or (B), any participation in the further processing of livestock which was raised in such trade or business (or in the trade or business referred to in subparagraph (A) or (B)),

(D) in the case of an individual whose principal business activity involves active participation in the management of a trade or business of farming, any interest in any other trade or business of farming, and,

(E) any interest held by a member of the family (or a spouse of any such member) of

a grandparent of an individual described in subparagraph (A), (B), (C), or (D) if the interest in the partnership or the enterprise is attributable to the active participation of the individual described in subparagraph (A), (B), (C), or (D).

For purposes of subparagraph (A), where one farm is substituted for or added to another farm, both farms shall be treated as one farm. For purposes of subparagraph (E), the term ''family'' has the meaning given to such term by section 267(c)(4).

(3) Farming

For purposes of this subsection, the term ''farming'' has the meaning given to such term by section 464(e).

(4) Limited entrepreneur

For purposes of this subsection, the term ''limited entrepreneur'' means a person who—

(A) has an interest in an enterprise other than as a limited partner, and

(B) does not actively participate in the management of such enterprise.

***(l)* Limitation on excess business losses of noncorporate taxpayers**

(1) Limitation

In the case of a taxpayer other than a corporation—

(A) for any taxable year beginning after December 31, 2017, and before January 1, 2026, subsection (j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and

(B) for any taxable year beginning after December 31, 2020, and before January 1, 2026, any excess business loss of the taxpayer for the taxable year shall not be allowed.

(2) Disallowed loss carryover

Any loss which is disallowed under paragraph (1) shall be treated as a net operating loss for the taxable year for purposes of determining any net operating loss carryover under section 172(b) for subsequent taxable years.

(3) Excess business loss

For purposes of this subsection—

(A) In general

The term ''excess business loss'' means the excess (if any) of—

(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to trades or businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1) and without regard to any deduction allowable under section 172 or 199A), over

(ii) the sum of—

(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such trades or businesses, plus

(II) $250,000 (200 percent of such amount in the case of a joint return).

Such excess shall be determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee.

(B) Treatment of capital gains and losses

(i) Losses

Deductions for losses from sales or exchanges of capital assets shall not be taken into account under subparagraph (A)(i).

(ii) Gains

The amount of gains from sales or exchanges of capital assets taken into account under subparagraph (A)(ii) shall not exceed the lesser of—

(I) the capital gain net income determined by taking into account only gains and losses attributable to a trade or business, or

(II) the capital gain net income.

(C) Adjustment for inflation

In the case of any taxable year beginning after December 31, 2018, the $250,000 amount in subparagraph (A)(ii)(II) shall be increased by an amount equal to—

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting ''2017'' for ''2016'' in subparagraph (A)(ii) thereof.

If any amount as increased under the preceding sentence is not a multiple of $1,000, such amount shall be rounded to the nearest multiple of $1,000.

(4) Application of subsection in case of partnerships and S corporations

In the case of a partnership or S corporation—

(A) this subsection shall be applied at the partner or shareholder level, and

(B) each partner's or shareholder's allocable share of the items of income, gain, deduction, or loss of the partnership or S corporation for any taxable year from trades or businesses attributable to the partnership or S corporation shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

For purposes of this paragraph, in the case of an S corporation, an allocable share shall be the shareholder's pro rata share of an item.

(5) Additional reporting

The Secretary shall prescribe such additional reporting requirements as the Secretary determines necessary to carry out the purposes of this subsection.

(6) Coordination with section 469

This subsection shall be applied after the application of section 469.

(Aug. 16, 1954, ch. 736, 68A Stat. 157; Pub. L. 86–781, §6(a), Sept. 14, 1960, 74 Stat. 1020; Pub. L. 87–876, §3(a), Oct. 24, 1962, 76 Stat. 1199; Pub. L. 88–272, title II, §223(a)(1), Feb. 26, 1964, 78 Stat.

76; Pub. L. 94–455, title II, §208(a), title XIX, §§1901(a)(69), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1541, 1775, 1834; Pub. L. 98–369, div. A, title I, §91(a), (e), July 18, 1984,98 Stat. 598, 607; Pub. L. 99–514, title VIII, §§801(b), 805(c)(5), 823(b)(1), title XVIII, §1807(a)(1), (2), Oct. 22, 1986, 100 Stat. 2347, 2362, 2374, 2811; Pub. L. 100–203, title X, §10201(b)(5), Dec. 22, 1987, 101 Stat. 1330–387; Pub. L. 100–647, title I, §§1008(a)(3), 1018(u)(5), Nov. 10, 1988, 102 Stat. 3436, 3590; Pub. L. 101–239, title VII, §7721(c)(10), Dec. 19, 1989, 103 Stat. 2400; Pub. L. 101–508, title XI, §11704(a)(5), Nov. 5, 1990, 104 Stat. 1388–518; Pub. L. 104–188, title I, §1704(t)(24), (78), Aug. 20, 1996, 110 Stat. 1888, 1891; Pub. L. 109–135, title IV, §412(aa), Dec. 21, 2005, 119 Stat. 2638; Pub. L. 110–234, title XV, §15351(a), May 22, 2008, 122 Stat. 1523; Pub. L. 110–246, §4(a), title XV, §15351(a), June 18, 2008, 122 Stat. 1664, 2285; Pub. L. 113–295, div. A, title II, §221(a)(58)(B), Dec. 19, 2014, 128 Stat. 4047; Pub. L. 115–97, title I, §11012(a), Dec. 22, 2017, 131 Stat. 2071; Pub. L. 115–141, div. U, title IV, §401(a)(117), Mar. 23, 2018, 132 Stat. 1190; Pub. L. 116–136, div. A, title II, §2304(a), (b), Mar. 27, 2020, 134 Stat. 356.)

Inflation Adjusted Items for Certain Years

For inflation adjustment of certain items in this section, see Revenue Procedures listed in a table under section 1 of this title.

References in Text

The Food, Conservation, and Energy Act of 2008, referred to in subsec. (j)(3)(A), is Pub. L. 110–246, June 18, 2008, 122 Stat. 1651. Title I of the Act is classified principally to chapter 113 (§8701 et seq.) of Title 7, Agriculture. For complete classification of this Act to the Code, see Short Title note set out under section 8701 of Title 7 and Tables.

Codification

Subsec. (c) of section 464 of this title, which was transferred to this section and redesignated subsec. (j) by Pub. L. 113–295, §221(a)(58)(B)(i), was based on Pub. L. 94–455, title II, §207(a)(1), Oct. 4, 1976, 90 Stat. 1536.

Pub. L. 110–234 and Pub. L. 110–246 made identical amendments to this section. The amendments by Pub. L. 110–234 were repealed by section 4(a) of Pub. L. 110–246.

Amendments

2020—Subsec. (*l*)(1). Pub. L. 116–136, §2304(a), amended par. (1) generally. Prior to amendment, text read as follows: ''In the case of taxable year of a taxpayer other than a corporation beginning after December 31, 2017, and before January 1, 2026—

''(A) subsection (j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and

''(B) any excess business loss of the taxpayer for the taxable year shall not be allowed.''

Subsec. (*l*)(2). Pub. L. 116–136, §2304(b)(1), substituted ''a net operating loss for the taxable year for purposes of determining any net operating loss carryover under section 172(b) for subsequent taxable years'' for ''a net operating loss carryover to the following taxable year under section 172''.

Subsec. (*l*)(3)(A). Pub. L. 116–136, §2304(b)(2)(B), inserted concluding provisions.

Subsec. (*l*)(3)(A)(i). Pub. L. 116–136, §2304(b)(2)(A), inserted ''and without regard to any deduction allowable under section 172 or 199A'' after ''under paragraph (1)''.

Subsec. (*l*)(3)(B), (C). Pub. L. 116–136, §2304(b)(3), added subpar. (B) and redesignated former subpar. (B) as (C).

2018—Subsec. (i)(4). Pub. L. 115–141, §401(a)(117)(B), substituted ''subsection (k)'' for ''subsection (j)''.

Subsecs. (j), (k). Pub. L. 115–141, §401(a)(117)(A), redesignated subsec. (j) relating to farming syndicate defined as (k).

2017—Subsec. (*l*). Pub. L. 115–97 added subsec. (*l*).

2014—Subsec. (i)(4). Pub. L. 113–295, §221(a)(58)(B)(iii), substituted ''subsection (j)'' for ''section 464(c)''.

Subsec. (j). Pub. L. 113–295, §221(a)(58)(B)(i), transferred subsec. (c) of section 464 of this title, relating to farming syndicate defined, to the end of this section and redesignated it as subsec. (j).

Subsec. (j)(1). Pub. L. 113–295, §221(a)(58)(B)(ii)(I), substituted ''For purposes of subsection (i)(4)'' for ''For purposes of this section'' in introductory provisions.

Subsec. (j)(3), (4). Pub. L. 113–295, §221(a)(58)(B)(ii)(II), added pars. (3) and (4).

2008—Subsec. (j). Pub. L. 110–246, §15351(a), added subsec. (j) relating to limitation on excess farm losses of certain taxpayers.

2005—Subsec. (i)(3)(C). Pub. L. 109–135 substituted ''section 6662(d)(2)(C)(ii)'' for ''section 6662(d)(2)(C)(iii)''.

1996—Subsec. (i)(3)(C). Pub. L. 104–188, §1704(t)(78), substituted ''section 6662(d)(2)(C)(iii)'' for ''section 6662(d)(2)(C)(ii)''.

Pub. L. 104–188, §1704(t)(24), amended directory language of Pub. L. 101–239. See 1989 Amendment note below.

1990—Subsec. (i)(3)(C). Pub. L. 101–508 amended subpar. (C) generally. Prior to amendment, subpar. (C) read as follows: ''any tax shelter (within the meaning of section 6662(d)(2)(C)(ii)).''

1989—Subsec. (i)(3)(C). Pub. L. 101–239, as amended by Pub. L. 104–188, §1704(t)(24), substituted ''section 6662(d)(2)(C)(ii)'' for ''section 6661(b)(2)(C)(ii)''.

1988—Subsec. (h)(5)(B), (C). Pub. L. 100–647, §1018(u)(5), amended Pub. L. 99–514, §823(b)(1). See 1986 Amendment note below.

Subsec. (i)(2). Pub. L. 100–647, §1008(a)(3), amended par. (2) generally. Prior to amendment, par. (2) read as follows: ''In the case of a tax shelter, economic performance with respect to the act of drilling an oil or gas well shall be treated as having occurred within a taxable year if drilling of the well commences before the close of the 90th day after the close of the taxable year.''

1987—Subsec. (h)(5). Pub. L. 100–203 substituted ''items'' for ''cases to which other provisions of this title specifically apply'' in heading and amended text generally. Prior to amendment, text read as follows: ''This subsection shall not apply to any item to which any of the following provisions apply:

''(A) Section 463 (relating to vacation pay).

''(B) Any other provisions of this title which specifically provides for a deduction for a reserve for estimated expenses.''

1986—Subsec. (h)(5)(A). Pub. L. 99–514, §805(c)(5), redesignated subpar. (B) as (A) and struck out former subpar. (A) which referred to subsec. (c) or (f) of section 166.

Subsec. (h)(5)(B). Pub. L. 99–514, §823(b)(1), as amended by Pub. L. 100–647, §1018(u)(5), redesignated subpar. (C) as (B) and struck out former subpar. (B) which read as follows: ''Section 466 (relating to discount coupons).''

Pub. L. 99–514, §805(c)(5), redesignated subpar. (C) as (B). Former subpar. (B) redesignated (A).

Subsec. (h)(5)(C). Pub. L. 99–514, §823(b)(1), as amended by Pub. L. 100–647, §1018(u)(5), redesignated subpar. (C) as (B).

Pub. L. 99–514, §805(c)(5), redesignated subpar. (D) as (C). Former subpar. (C) redesignated (B).

Subsec. (h)(5)(D). Pub. L. 99–514, §805(c)(5), redesignated subpar. (D) as (C).

Subsec. (i). Pub. L. 99–514, §801(b)(1), substituted ''Special rules for tax shelters'' for ''Tax shelters may not deduct items earlier than when economic performance occurs'' in heading.

Subsec. (i)(1). Pub. L. 99–514, §801(b)(1), substituted ''Recurring item exception not to apply'' for ''In general'' in heading and amended par. (1) generally. Prior to amendment, par. (1) read as follows: ''In the case of a tax shelter computing taxable income under the cash receipts and disbursements method of accounting, such tax shelter shall not be allowed a deduction under this

chapter with respect to any item any earlier than the time when such item would be treated as incurred under subsection (h) (determined without regard to paragraph (3) thereof).''

Subsec. (i)(2). Pub. L. 99–514, §801(b)(1), amended par. (2) generally, substituting provisions relating to special rule for spudding of oil or gas wells for former provisions consisting of subpars. (A) to (D) which related to deduction of items when economic performance occurs on or before 90th day after close of the taxable year to the extent of cash basis.

Pub. L. 99–514, §1807(a)(1), substituted ''on or before the 90th day'' for ''within 90 days'' in heading and substituted ''before the close of the 90th day after the close of the taxable year'' for ''within 90 days after the close of the taxable year'' in subpar. (A).

Subsec. (i)(4). Pub. L. 99–514, §801(b)(2), amended par. (4) generally. Prior to amendment, par. (4) read as follows: ''In the case of the trade or business of farming (as defined in section 464(e))—

''(A) any tax shelter described in paragraph (3)(C) shall be treated as a farming syndicate for purposes of section 464; except that this subparagraph shall not apply for purposes of determining the income of an individual meeting the requirements of section 464(c)(2),

''(B) section 464 shall be applied before this subsection, and

''(C) in determining whether an entity is a tax shelter, the definition of farming syndicate in section 464(c) shall be substituted for subparagraphs (A) and (B) of paragraph (3).''

Subsec. (i)(4)(A). Pub. L. 99–514, §1807(a)(2), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''section 464 shall be applied to any tax shelter described in paragraph (3)(C),''.

1984—Subsec. (f)(4). Pub. L. 98–369, §91(e), inserted ''determined after application of subsection (h)''.

Subsecs. (h), (i). Pub. L. 98–369, §91(a), added subsecs. (h) and (i).

1976—Subsec. (c)(2), (3). Pub. L. 94–455, §§1901(a)(69)(A), (B), 1906(b)(13)(A), redesignated par. (3) as (2), substituted ''in which he'' for ''which begins after December 31, 1953, and ends after the date of the enactment of this title in which the taxpayer'', and struck out ''or his delegate'' after ''Secretary'' wherever appearing. Former par. (2), which related to special limitations on the applicability of par. (1), was struck out.

Subsecs. (d), (e). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary'' wherever appearing.

Subsec. (g). Pub. L. 94–455, §208(a), added subsec. (g).

1964—Subsec. (f). Pub. L. 88–272 added subsec. (f).

1962—Subsec. (e). Pub. L. 87–876 added subsec. (e).

1960—Subsec. (d). Pub. L. 86–781 added subsec. (d).

EFFECTIVE DATE OF 2020 AMENDMENT

Pub. L. 116–136, div. A, title II, §2304(c), Mar. 27, 2020, 134 Stat. 356, provided that:

''(1) IN GENERAL.—The amendments made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 2017.

''(2) TECHNICAL AMENDMENTS.—The amendments made by subsection (b) [amending this section] shall take effect as if included in the provisions of Public Law 115–97 to which they relate.''

EFFECTIVE DATE OF 2017 AMENDMENT

Pub. L. 115–97, title I, §11012(b), Dec. 22, 2017, 131 Stat. 2072, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2017.''

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 2008 AMENDMENT

Amendment of this section and repeal of Pub. L. 110–234 by Pub. L. 110–246 effective May 22, 2008, the date of enactment of Pub. L. 110–234, except as otherwise provided, see section 4 of Pub. L. 110–246, set out as an Effective Date note under section 8701 of Title 7, Agriculture.

Pub. L. 110–234, title XV, §15351(b), May 22, 2008, 122 Stat. 1525, and Pub. L. 110–246, §4(a), title XV, §15351(b), June 18, 2008, 122 Stat. 1664, 2287, provided that: ''The amendment made by this section [amending this section] shall apply to taxable years beginning after December 31, 2009.''

[Pub. L. 110–234 and Pub. L. 110–246 enacted identical provisions. Pub. L. 110–234 was repealed by section 4(a) of Pub. L. 110–246, set out as a note under section 8701 of Title 7, Agriculture.]

EFFECTIVE DATE OF 1989 AMENDMENT

Pub. L. 101–239, title VII, §7721(d), Dec. 19, 1989, 103 Stat. 2400, provided that: ''The amendments made by this section [enacting sections 6662 to 6665 of this title, amending this section and sections 1274, 5684, 5761, 6013, 6222, 6601, 6621, 6653, 6672, and 7519 of this title, and repealing sections 6659, 6659A, 6660, 6661, and former section 6662 of this title] shall apply to returns the due date for which (determined without regard to extensions) is after December 31, 1989.''

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1987 AMENDMENT

Amendment by Pub. L. 100–203 applicable to taxable years beginning after Dec. 31, 1987, see section 10201(c)(1) of Pub. L. 100–203, set out as a note under section 404 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 801(b) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, with certain exceptions and qualifications, see section 801(d) of Pub. L. 99–514, set out as an Effective Date note under section 448 of this title.

Amendment by section 805(c)(5) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, with certain changes required in method of accounting, see section 805(d) of Pub. L. 99–514, set out as a note under section 166 of this title.

Amendment by section 823 of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, with changes required in the method of accounting, see section 823(c) of Pub. L. 99–514, set out as an Effective Date of Repeal note under section 466 of this title.

Amendment by section 1807(a)(1), (2) of Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Pub. L. 98–369, div. A, title I, §91(g)–(i), July 18, 1984, 98 Stat. 608, 609, as amended by Pub. L. 99–514, §2, title XVIII, §1807(a)(3)(B), (4)(F), (5), (6), Oct. 22, 1986, 100 Stat. 2095, 2811, 2813, 2814, provided that:

''(g) EFFECTIVE DATES.—

''(1) IN GENERAL.—Except as provided in this subsection and subsections (h) and (i), the amendments made by this section [enacting sections 88, 468, and 468A of this title and amending this section and section 172 of this title] shall apply to amounts with respect to which a deduction would be allowable under chapter 1 of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (determined without regard to such amendments) after—

''(A) in the case of amounts to which section 461(h) of such Code (as added by such amendments)

applies, the date of the enactment of this Act [July 18, 1984], and

''(B) in the case of amounts to which section 461(i) of such Code (as so added) applies, after March 31, 1984.

''(2) TAXPAYER MAY ELECT EARLIER APPLICATION.—

''(A) IN GENERAL.—In the case of amounts described in paragraph (1)(A), a taxpayer may elect to have the amendments made by this section apply to amounts which—

''(i) are incurred on or before the date of the enactment of this Act [July 18, 1984] (determined without regard to such amendments), and

''(ii) are incurred after the date of the enactment of this Act (determined with regard to such amendments).

The Secretary of the Treasury or his delegate may by regulations provide that (in lieu of an election under the preceding sentence) a taxpayer may (subject to such conditions as such regulations may provide) elect to have subsection (h) of section 461 of such Code apply to the taxpayer's entire taxable year in which occurs July 19, 1984.

''(B) ELECTION TREATED AS CHANGE IN THE METHOD OF ACCOUNTING.—For purposes of section 481 of the Internal Revenue Code of 1986, if an election is made under subparagraph (A) with respect to any amount, the application of the amendments made by this section shall be treated as a change in method of accounting—

''(i) initiated by the taxpayer,

''(ii) made with the consent of the Secretary of the Treasury, and

''(iii) with respect to which section 481 of such Code shall be applied by substituting a 3-year adjustment period for a 10-year adjustment period.

''(3) SECTION 461(h) TO APPLY IN CERTAIN CASES.—Notwithstanding paragraph (1), section 461(h) of the Internal Revenue Code of 1986 (as added by this section) shall be treated as being in effect to the extent necessary to carry out any amendments made by this section which take effect before section 461(h).

''(4) EFFECTIVE DATE FOR TREATMENT OF MINING AND SOLID WASTE RECLAMATION AND CLOSING COSTS.—Except as otherwise provided in subsection (h), the amendments made by subsection (b) [enacting section 468 of this title] shall take effect on the date of the enactment of this Act [July 18, 1984] with respect to taxable years ending after such date.

''(5) RULES FOR NUCLEAR DECOMMISSIONING COSTS.—The amendments made by subsections (c) and (f) [enacting sections 88 and 468A of this title] shall take effect on the date of the enactment of this Act [July 18, 1984] with respect to taxable years ending after such date.

''(6) MODIFICATION OF NET OPERATING LOSS CARRYBACK PERIOD.—The amendments made by subsection (d) [amending section 172 of this title] shall apply to losses for taxable years beginning after December 31, 1983.

''(h) EXCEPTION FOR CERTAIN EXISTING ACTIVITIES AND CONTRACTS.—If—

''(1) EXISTING ACCOUNTING PRACTICES.—If, on March 1, 1984, any taxpayer was regularly computing his deduction for mining reclamation activities under a current cost method of accounting (as determined by the Secretary of the Treasury or his delegate), the liability for reclamation activities—

''(A) for land disturbed before the date of the enactment of this Act [July 18, 1984], or

''(B) to which paragraph (2) applies,

shall be treated as having been incurred when the land was disturbed.

''(2) FIXED PRICE SUPPLY CONTRACT.—

''(A) IN GENERAL.—In the case of any fixed price supply contract entered into before March 1, 1984, the amendments made by subsection (b) [enacting section 468 of this title] shall not apply to any minerals extracted from such property which are sold pursuant to such contract.

''(B) NO EXTENSION OR RENEGOTIATION.—Subparagraph (A) shall not apply—

''(i) to any extension of any contract beyond the period such contract was in effect on March 1, 1984, or

''(ii) to any renegotiation of, or other change in, the terms and conditions of such contract in effect on March 1, 1984.

''(i) TRANSITIONAL RULE FOR ACCRUED VACATION PAY.—

''(1) IN GENERAL.—In the case of any taxpayer—

''(A) with respect to whom a deduction was allowable (other than under section 463 of the Internal Revenue Code of 1986) for vested accrued vacation pay for the last taxable year ending before the date of the enactment of this Act [July 18, 1984], and

''(B) who elects the application of section 463 of such Code for the first taxable year ending after the date of the enactment of this Act,

then, for purposes of section 463(b) of such Code, the opening balance of the taxpayer with respect to any vested accrued vacation pay shall be determined under section 463(b)(1) of such Code.

''(2) VESTED ACCRUED VACATION PAY.—For purposes of this subsection, the term 'vested accrued vacation pay' means any amount allowable under section 162(a) of such Code with respect to vacation pay of employees of the taxpayer (determined without regard to section 463 of such Code).''

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(69) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

Pub. L. 94–455, title II, § 208(b), Oct. 4, 1976, 90 Stat. 1542, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendment made by subsection (a) [amending this section] shall apply to amounts paid after December 31, 1975, in taxable years ending after such date.

''(2) CERTAIN AMOUNTS PAID BEFORE 1977.—The amendment made by subsection (a) [amending this section] shall not apply to amounts paid before January 1, 1977, pursuant to a binding contract or written loan commitment which existed on September 16, 1975 (and at all times thereafter), and which required prepayment of such amounts by the taxpayer.''

EFFECTIVE DATE OF 1964 AMENDMENT

Pub. L. 88–272, title II, § 223(b), Feb. 26, 1964, 78 Stat. 76, provided that: ''Except as provided in subsections (c) and (d) [set out below]—

''(1) the amendment made by subsection (a)(1) [amending this section] shall apply to taxable years beginning after December 31, 1953, and ending after August 16, 1954, and

''(2) the amendment made by subsection (a)(2) [amending section 43 of the Internal Revenue Code of 1939] shall apply to taxable years to which the Internal Revenue Code of 1939 applies.''

EFFECTIVE DATE OF 1962 AMENDMENT

Pub. L. 87–876, § 3(b), Oct. 24, 1962, 76 Stat. 1199, provided that: ''The amendment made by subsection (a) [amending this section] shall apply only with respect to taxable years ending after December 31, 1962.''

EFFECTIVE DATE OF 1960 AMENDMENT

Pub. L. 86–781, § 6(b), Sept. 14, 1960, 74 Stat. 1021, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years ending after December 31, 1960.''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147

and 1171–1177] or title XVIII [§§1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

TRANSITIONAL RULE FOR CERTAIN AMOUNTS

Pub. L. 99–514, title XVIII, §1807(a)(8), Oct. 22, 1986, 100 Stat. 2816, provided that: ''For purposes of section 461(h) of the Internal Revenue Code of 1954 [now 1986], economic performance shall be treated as occurring on the date of a payment to an insurance company if—

''(A) such payment was made before November 23, 1985, for indemnification against a tort liability relating to personal injury or death caused by inhalation or ingestion of dust from asbestos-containing insulation products,

''(B) such insurance company is unrelated to taxpayer,

''(C) such payment is not refundable, and

''(D) the taxpayer is not engaged in the mining of asbestos nor is any member of any affiliated group which includes the taxpayer so engaged.''

TRANSITION RULE

Pub. L. 99–514, title XVIII, §1807(c), Oct. 22, 1986, 100 Stat. 2817, provided that: ''A taxpayer shall be allowed to use the cash receipts and disbursements method of accounting for taxable years ending after January 1, 1982, if such taxpayer—

''(1) is a partnership which was founded in 1936,

''(2) has over 1,000 professional employees,

''(3) used a long-term contract method of accounting for a substantial part of its income from the performance of architectural and engineering services, and

''(4) is headquartered in Chicago, Illinois.''

ELECTION AS TO TRANSFERS IN TAXABLE YEARS BEGINNING BEFORE JAN. 1, 1964

Pub. L. 88–272, title II, §223(c), Feb. 26, 1964, 78 Stat. 76, provided that:

''(1) The amendments made by subsection (a) [amending this section and section 43 of the Internal Revenue Code of 1939] shall not apply to any transfer of money or other property described in subsection (a) made in a taxable year beginning before January 1, 1964, if the taxpayer elects, in the manner provided by regulations prescribed by the Secretary of the Treasury or his delegate, to have this paragraph apply. Such an election—

''(A) must be made within one year after the date of the enactment of this Act [Feb. 26, 1964],

''(B) may not be revoked after the expiration of such one-year period, and

''(C) shall apply to all transfers described in the first sentence of this paragraph (other than transfers described in paragraph (2)).

In the case of any transfer to which this paragraph applies, the deduction shall be allowed only for the taxable year in which the contest with respect to such transfer is settled.

''(2) Paragraph (1) shall not apply to any transfer if the assessment of any deficiency which would result from the application of the election in respect of such transfer is, on the date of the election under paragraph (1), prevented by the operation of any law or rule of law.

''(3) If the taxpayer makes an election under paragraph (1), and if, on the date of such election, the assessment of any deficiency which results from the application of the election in respect of any transfer is not prevented by the operation of any law or rule of law, the period within which assessment of such deficiency may be made shall not expire earlier than 2 years after the date of the enactment of this Act [Feb. 26, 1964].''

CERTAIN OTHER TRANSFERS IN TAXABLE YEARS BEGINNING BEFORE JAN. 1, 1964

Pub. L. 88–272, title II, §223(d), Feb. 26, 1964, 78 Stat. 77, provided that: ''The amendments made by subsection (a) [amending this section and section 43 of the Internal Revenue Code of 1939] shall not apply to any transfer of money or other property described in subsection (a) made in a taxable year beginning before January 1, 1964, if—

''(1) no deduction has been allowed in respect of such transfer for any taxable year before the taxable year in which the contest with respect to such transfer is settled, and

''(2) refund or credit of any overpayment which would result from the application of such amendments to such transfer is prevented by the operation of any law or rule of law.

In the case of any transfer to which this subsection applies, the deduction shall be allowed for the taxable year in which the contest with respect to such transfer is settled.''

[§ 462. Repealed. June 15, 1955, ch. 143, § 1(b), 69 Stat. 134]

Section, act Aug. 16, 1954, ch. 736 68A Stat. 158, related to reserves for estimated expenses.

EFFECTIVE DATE OF REPEAL

Repeal effective with respect to taxable years beginning after Dec. 31, 1953, and ending after Aug. 16, 1954, see section 3 of Act June 15, 1955, set out as an Effective Date of 1955 Amendment note under section 381 of this title.

SAVINGS PROVISION

For provisions concerning increase in tax in any taxable year ending on or before June 15, 1955 by reason of enactment of act June 15, 1955, see section 4 of act June 15, 1955, set out as a note under section 381 of this title.

[§ 463. Repealed. Pub. L. 100–203, title X, § 10201(a), Dec. 22, 1987, 101 Stat. 1330–387]

Section, added Pub. L. 93–625, §4(a), Jan. 3, 1974, 88 Stat. 2109; amended Pub. L. 94–455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 98–369, div. A, title V, §561(a), July 18, 1984, 98 Stat. 901; Pub. L. 99–514, title XI, §1165(a), Oct. 22, 1986, 100 Stat. 2511, related to deduction allowable for accrual basis taxpayers under section 162(a) of this title with respect to vacation pay.

EFFECTIVE DATE OF REPEAL

Repeal applicable to taxable years beginning after Dec. 31, 1987, see section 10201(c)(1) of Pub. L. 100–203, set out as an Effective Date of 1987 Amendment note under section 404 of this title.

CHANGE IN METHOD OF ACCOUNTING REQUIRED BY PUB. L. 100–203

Pub. L. 100–203, title X, §10201(c)(2), Dec. 22, 1987, 101 Stat. 1330–388, provided that: ''In the case of any taxpayer who elected to have section 463 of the Internal Revenue Code of 1986 apply for such taxpayer's last taxable year beginning before January 1, 1988, and who is required to change his method of accounting by reason of the amendments made by this section [amending sections 404, 419, and 461 of this title, repealing sections 81 and 463 of this title, and enacting provisions set out as a note under section 404 of this title]—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as having been made with the consent of the Secretary, and

''(C) the net amount of adjustments required by section 481 of such Code to be taken into account by the taxpayer—

''(i) shall be reduced by the balance in the suspense account under section 463(c) of such Code as of the close of such last taxable year, and

''(ii) shall be taken into account over the 4-taxable year period beginning with the taxable year following such last taxable year as follows:

"In the case of the:	The percentage taken into account is:
1st year	25
2nd year	5
3rd year	35
4th year	35.

Notwithstanding subparagraph (C)(ii), if the period the adjustments are required to be taken into account under section 481 of such Code is less than 4 years, such adjustments shall be taken into account ratably over such shorter period.''

§ 464. Limitations on deductions for certain farming expenses

(a) General rule

In the case of any taxpayer to whom subsection (d) applies, a deduction (otherwise allowable under this chapter) for amounts paid for feed, seed, fertilizer, or other similar farm supplies shall only be allowed for the taxable year in which such feed, seed, fertilizer, or other supplies are actually used or consumed, or, if later, for the taxable year for which allowable as a deduction (determined without regard to this section).

(b) Certain poultry expenses

In the case of any taxpayer to whom subsection (d) applies—

(1) the cost of poultry (including egg-laying hens and baby chicks) purchased for use in a trade or business (or both for use in a trade or business and for sale) shall be capitalized and deducted ratably over the lesser of 12 months or their useful life in the trade or business, and

(2) the cost of poultry purchased for sale shall be deducted for the taxable year in which the poultry is sold or otherwise disposed of.

(c) Exception

Subsection (a) shall not apply to any amount paid for supplies which are on hand at the close of the taxable year on account of fire, storm, or other casualty, or on account of disease or drought.

(d) Certain persons prepaying 50 percent or more of certain farming expenses

(1) Taxpayer to whom subsection applies

This subsection applies to any taxpayer for any taxable year if such taxpayer—

(A) does not use an accrual method of accounting,

(B) has excess prepaid farm supplies for the taxable year, and

(C) is not a qualified farm-related taxpayer.

(2) Qualified farm-related taxpayer

(A) In general

For purposes of this subsection, the term ''qualified farm-related taxpayer'' means any farm-related taxpayer if—

(i)(I) the aggregate prepaid farm supplies for the 3 taxable years preceding the taxable year are less than 50 percent of,

(II) the aggregate deductible farming expenses (other than prepaid farm supplies) for such 3 taxable years, or

(ii) the taxpayer has excess prepaid farm supplies for the taxable year by reason of any change in business operation directly attributable to extraordinary circumstances.

(B) Farm-related taxpayer

For purposes of this paragraph, the term ''farm-related taxpayer'' means any taxpayer—

(i) whose principal residence (within the meaning of section 121) is on a farm,

(ii) who has a principal occupation of farming, or

(iii) who is a member of the family (within the meaning of section 461(k)(2)(E)) of a taxpayer described in clause (i) or (ii).

(3) Definitions

For purposes of this subsection—

(A) Excess prepaid farm supplies

The term ''excess prepaid farm supplies'' means the prepaid farm supplies for the taxable year to the extent the amount of such supplies exceeds 50 percent of the deductible farming expenses for the taxable year (other than prepaid farm supplies).

(B) Prepaid farm supplies

The term ''prepaid farm supplies'' means any amounts which are described in subsection (a) or (b) and would be allowable for a subsequent taxable year under the rules of subsections (a) and (b).

(C) Deductible farming expenses

The term ''deductible farming expenses'' means any amount allowable as a deduction under this chapter (including any amount allowable as a deduction for depreciation or amortization) which is properly allocable to the trade or business of farming.

(e) Farming

For purposes of this section, the term ''farming'' means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity including the raising, shearing, feeding, caring for, training, and management of animals. For purposes of the preceding sentence, trees (other than trees bearing fruit or nuts) shall not be treated as an agricultural or horticultural commodity.

(Added Pub. L. 94–455, title II, § 207(a)(1), Oct. 4, 1976, 90 Stat. 1536; amended Pub. L. 95–600, title VII, § 701(*l*)(3), Nov. 6, 1978, 92 Stat. 2907; Pub. L. 97–354, § 5(a)(30), Oct. 19, 1982, 96 Stat. 1695; Pub. L. 99–514, title IV, § 404(a), (b)(1), title VIII, § 803(b)(8), Oct. 22, 1986, 100 Stat. 2223, 2224, 2356; Pub. L. 100–647, title I, § 1008(a)(4), Nov. 10, 1988, 102 Stat. 3437; Pub. L. 105–34, title III, § 312(d)(1), Aug. 5, 1997, 111 Stat. 839; Pub. L. 113–295, div. A, title II, § 221(a)(58)(A), (B)(i), (C), (D), Dec. 19, 2014, 128 Stat. 4047; Pub. L. 115–141, div. U, title IV, § 401(a)(118), (119), Mar. 23, 2018, 132 Stat. 1190.)

AMENDMENTS

2018—Pub. L. 115–141, § 401(a)(118), inserted ''expenses'' after ''farming'' in section catchline.

Subsec. (d)(2)(B)(iii). Pub. L. 115–141, § 401(a)(119), substituted ''section 461(k)(2)(E)'' for ''subsection (c)(2)(E)''.

2014—Subsecs. (a), (b). Pub. L. 113–295, § 221(a)(58)(A), substituted ''any taxpayer to whom subsection (d) applies'' for ''any farming syndicate (as defined in subsection (c))'' in subsec. (a) and in introductory provisions of subsec. (b).

Subsec. (c). Pub. L. 113–295, § 221(a)(58)(C)(i), redesignated subsec. (d) as (c). Former subsec. (c) transferred to section 461 of this title.

Pub. L. 113–295, § 221(a)(58)(B)(i), transferred subsec. (c) defining the term ''farming syndicate'' to section 461 of this title and redesignated it as subsec. (j) of that section.

Subsec. (d). Pub. L. 113–295, § 221(a)(58)(D), struck out ''Subsections (a) and (b) to apply to'' before ''Certain persons'' in heading, redesignated pars. (2) to (4) as (1) to (3), respectively, and struck out former par. (1). Prior to amendment, text of par. (1) read as follows: ''In the case of a taxpayer to whom this subsection applies, subsections (a) and (b) shall apply to the excess prepaid farm supplies of such taxpayer in the same manner as if such taxpayer were a farming syndicate.''

Pub. L. 113–295, § 221(a)(58)(C)(i), redesignated subsec. (f) as (d). Former subsec. (d) redesignated (c).

Subsec. (e). Pub. L. 113–295, § 221(a)(58)(C), added subsec. (e) and struck out former subsec. (e) which defined the terms ''farming'' and ''limited entrepreneur'' for purposes of this section.

Subsec. (f). Pub. L. 113–295, § 221(a)(58)(C)(i), redesignated subsec. (f) as (d).

Subsec. (g). Pub. L. 113–295, § 221(a)(58)(C)(i), struck out subsec. (g). Text read as follows: ''Except as provided in subsection (f), subsections (a) and (b) shall not apply to any taxable year beginning after December 31, 1986.''

1997—Subsec. (f)(3)(B)(i). Pub. L. 105–34 substituted ''section 121'' for ''section 1034''.

1988—Subsec. (g). Pub. L. 100–647 added subsec. (g).

1986—Pub. L. 99–514, § 404(b)(1), substituted ''for certain farming'' for ''in case of farming syndicates'' in section catchline.

Subsec. (d). Pub. L. 99–514, § 803(b)(8), substituted ''Exception'' for ''Exceptions'' as heading and amended text generally. Prior to amendment, text read as follows: ''Subsection (a) shall not apply to—

''(1) any amount paid for supplies which are on hand at the close of the taxable year on account of fire, storm, flood, or other casualty or on account of disease or drought, or

''(2) any amount required to be charged to capital account under section 278.''

Subsec. (f). Pub. L. 99–514, § 404(a), added subsec. (f).

1982—Subsec. (c)(1)(A), (B). Pub. L. 97–354 substituted ''an S corporation'' for ''an electing small business corporation (as defined in section 1371(b))''.

1978—Subsec. (c)(2). Pub. L. 95–600 substituted in subpar. (E) ''(or a spouse of any such member)'' for ''(within the meaning of section 267(c)(4))'' and provided that for purposes of subpar. (E) the term ''family'' has the meaning given to such term by section 267(c)(4).

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105–34 applicable to sales and exchanges after May 6, 1997, with certain exceptions, see section 312(d) of Pub. L. 105–34, set out as a note under section 121 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the amendment by section 803(b)(8) of Pub. L. 99–514 is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99–514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101–239, set out as an Effective Date note under section 263A of this title.

Pub. L. 99–514, title IV, § 404(c), Oct. 22, 1986, 100 Stat. 2224, provided that: ''The amendments made by this section [amending this section] shall apply to amounts paid or incurred after March 1, 1986, in taxable years beginning after such date.''

Amendment by section 803(b)(8) of Pub. L. 99–514 applicable to costs incurred after Dec. 31, 1986, in taxable years ending after such date, except as otherwise provided, see section 803(d) of Pub. L. 99–514, set out as an Effective Date note under section 263A of this title.

EFFECTIVE DATE OF 1982 AMENDMENT

Amendment by Pub. L. 97–354 applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97–354, set out as an Effective Date note under section 1361 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Amendment by Pub. L. 95–600 effective as if included in this section or section 447 of this title at the time of their enactment, Oct. 4, 1976, see section 701(*l*)(4) of Pub. L. 95–600, set out as a note under section 447 of this title.

EFFECTIVE DATE

Pub. L. 94–455, title II, § 207(a)(3), Oct. 4, 1976, 90 Stat. 1537, provided that:

''(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this subsection [enacting this section] shall apply to taxable years beginning after December 31, 1975.

''(B) TRANSITIONAL RULE.—In the case of a farming syndicate in existence on December 31, 1975, and for which there was no change of membership throughout its taxable year beginning in 1976, the amendments made by this subsection shall apply to taxable years beginning after December 31, 1976.''

§ 465. Deductions limited to amount at risk

(a) Limitation to amount at risk

(1) In general

In the case of—

(A) an individual, and

(B) a C corporation with respect to which the stock ownership requirement of paragraph (2) of section 542(a) is met,

engaged in an activity to which this section applies, any loss from such activity for the taxable year shall be allowed only to the extent of the aggregate amount with respect to which the taxpayer is at risk (within the meaning of subsection (b)) for such activity at the close of the taxable year.

(2) Deduction in succeeding year

Any loss from an activity to which this section applies not allowed under this section for the taxable year shall be treated as a deduction allocable to such activity in the first succeeding taxable year.

(3) Special rules for applying paragraph (1)(B)

For purposes of paragraph (1)(B)—

(A) section 544(a)(2) shall be applied as if such section did not contain the phrase ''or by or for his partner''; and

(B) sections 544(a)(4)(A) and 544(b)(1) shall be applied by substituting ''the corporation meet the stock ownership requirements of section 542(a)(2)'' for ''the corporation a personal holding company''.

(b) Amounts considered at risk

(1) In general

For purposes of this section, a taxpayer shall be considered at risk for an activity with respect to amounts including—

(A) the amount of money and the adjusted basis of other property contributed by the taxpayer to the activity, and

(B) amounts borrowed with respect to such activity (as determined under paragraph (2)).

(2) Borrowed amounts

For purposes of this section, a taxpayer shall be considered at risk with respect to amounts borrowed for use in an activity to the extent that he—

(A) is personally liable for the repayment of such amounts, or

(B) has pledged property, other than property used in such activity, as security for such borrowed amount (to the extent of the net fair market value of the taxpayer's interest in such property).

No property shall be taken into account as security if such property is directly or indirectly financed by indebtedness which is secured by property described in paragraph (1).

(3) Certain borrowed amounts excluded

(A) In general

Except to the extent provided in regulations, for purposes of paragraph (1)(B), amounts borrowed shall not be considered to be at risk with respect to an activity if such amounts are borrowed from any person who has an interest in such activity or from a related person to a person (other than the taxpayer) having such an interest.

(B) Exceptions

(i) Interest as creditor

Subparagraph (A) shall not apply to an interest as a creditor in the activity.

(ii) Interest as shareholder with respect to amounts borrowed by corporation

In the case of amounts borrowed by a corporation from a shareholder, subparagraph (A) shall not apply to an interest as a shareholder.

(C) Related person

For purposes of this subsection, a person (hereinafter in this paragraph referred to as the ''related person'') is related to any person if—

(i) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

(ii) the related person and such person are engaged in trades or business under common control (within the meaning of subsections (a) and (b) of section 52).

For purposes of clause (i), in applying section 267(b) or 707(b)(1), ''10 percent'' shall be substituted for ''50 percent''.

(4) Exception

Notwithstanding any other provision of this section, a taxpayer shall not be considered at risk with respect to amounts protected against loss through nonrecourse financing, guarantees, stop loss agreements, or other similar arrangements.

(5) Amounts at risk in subsequent years

If in any taxable year the taxpayer has a loss from an activity to which subsection (a) applies, the amount with respect to which a taxpayer is considered to be at risk (within the meaning of subsection (b)) in subsequent taxable years with respect to that activity shall be reduced by that portion of the loss which (after the application of subsection (a)) is allowable as a deduction.

(6) Qualified nonrecourse financing treated as amount at risk

For purposes of this section—

(A) In general

Notwithstanding any other provision of this subsection, in the case of an activity of holding real property, a taxpayer shall be considered at risk with respect to the taxpayer's share of any qualified nonrecourse financing which is secured by real property used in such activity.

(B) Qualified nonrecourse financing

For purposes of this paragraph, the term ''qualified nonrecourse financing'' means any financing—

(i) which is borrowed by the taxpayer with respect to the activity of holding real property,

(ii) which is borrowed by the taxpayer from a qualified person or represents a loan from any Federal, State, or local government or instrumentality thereof, or is guaranteed by any Federal, State, or local government,

(iii) except to the extent provided in regulations, with respect to which no person is personally liable for repayment, and

(iv) which is not convertible debt.

(C) Special rule for partnerships

In the case of a partnership, a partner's share of any qualified nonrecourse financing of such partnership shall be determined on the basis of the partner's share of liabilities of such partnership incurred in connection with such financing (within the meaning of section 752).

(D) Qualified person defined

For purposes of this paragraph—

(i) In general

The term ''qualified person'' has the meaning given such term by section 49(a)(1)(D)(iv).

(ii) Certain commercially reasonable financing from related persons

For purposes of clause (i), section 49(a)(1)(D)(iv) shall be applied without regard to subclause (I) thereof (relating to financing from related persons) if the fi-

nancing from the related person is commercially reasonable and on substantially the same terms as loans involving unrelated persons.

(E) Activity of holding real property

For purposes of this paragraph—

(i) Incidental personal property and services

The activity of holding real property includes the holding of personal property and the providing of services which are incidental to making real property available as living accommodations.

(ii) Mineral property

The activity of holding real property shall not include the holding of mineral property.

(c) Activities to which section applies

(1) Types of activities

This section applies to any taxpayer engaged in the activity of—

(A) holding, producing, or distributing motion picture films or video tapes,

(B) farming (as defined in section 464(e)),

(C) leasing any section 1245 property (as defined in section 1245(a)(3)),

(D) exploring for, or exploiting, oil and gas resources, or

(E) exploring for, or exploiting, geothermal deposits (as defined in section 613(e)(2))[1]

as a trade or business or for the production of income.

(2) Separate activities

For purposes of this section—

(A) In general

Except as provided in subparagraph (B), a taxpayer's activity with respect to each—

(i) film or video tape,

(ii) section 1245 property which is leased or held for leasing,

(iii) farm,

(iv) oil and gas property (as defined under section 614), or

(v) geothermal property (as defined under section 614),

shall be treated as a separate activity.

(B) Aggregation rules

(i) Special rule for leases of section 1245 property by partnerships or S corporations

In the case of any partnership or S corporation, all activities with respect to section 1245 properties which—

(I) are leased or held for lease, and

(II) are placed in service in any taxable year of the partnership or S corporation,

shall be treated as a single activity.

(ii) Other aggregation rules

Rules similar to the rules of subparagraphs (B) and (C) of paragraph (3) shall apply for purposes of this paragraph.

[1] So in original. Probably should be followed by a comma.

(3) Extension to other activities

(A) In general

This section also applies to each activity—

(i) engaged in by the taxpayer in carrying on a trade or business or for the production of income, and

(ii) which is not described in paragraph (1).

(B) Aggregation of activities where taxpayer actively participates in management of trade or business

Except as provided in subparagraph (C), for purposes of this section, activities described in subparagraph (A) which constitute a trade or business shall be treated as one activity if—

(i) the taxpayer actively participates in the management of such trade or business, or

(ii) such trade or business is carried on by a partnership or an S corporation and 65 percent or more of the losses for the taxable year is allocable to persons who actively participate in the management of the trade or business.

(C) Aggregation or separation of activities under regulations

The Secretary shall prescribe regulations under which activities described in subparagraph (A) shall be aggregated or treated as separate activities.

(D) Application of subsection (b)(3)

In the case of an activity described in subparagraph (A), subsection (b)(3) shall apply only to the extent provided in regulations prescribed by the Secretary.

(4) Exclusion for certain equipment leasing by closely-held corporations

(A) In general

In the case of a corporation described in subsection (a)(1)(B) actively engaged in equipment leasing—

(i) the activity of equipment leasing shall be treated as a separate activity, and

(ii) subsection (a) shall not apply to losses from such activity.

(B) 50-percent gross receipts test

For purposes of subparagraph (A), a corporation shall not be considered to be actively engaged in equipment leasing unless 50 percent or more of the gross receipts of the corporation for the taxable year is attributable, under regulations prescribed by the Secretary, to equipment leasing.

(C) Component members of controlled group treated as a single corporation

For purposes of subparagraph (A), the component members of a controlled group of corporations shall be treated as a single corporation.

(5) Waiver of controlled group rule where there is substantial leasing activity

(A) In general

In the case of the component members of a qualified leasing group, paragraph (4) shall be applied—

(i) by substituting ''80 percent'' for ''50 percent'' in subparagraph (B) thereof, and

(ii) as if paragraph (4) did not include subparagraph (C) thereof.

(B) Qualified leasing group

For purposes of this paragraph, the term ''qualified leasing group'' means a controlled group of corporations which, for the taxable year and each of the 2 immediately preceding taxable years, satisfied each of the following 3 requirements:

(i) At least 3 employees

During the entire year, the group had at least 3 full-time employees substantially all of the services of whom were services directly related to the equipment leasing activity of the qualified leasing members.

(ii) At least 5 separate leasing transactions

During the year, the qualified leasing members in the aggregate entered into at least 5 separate equipment leasing transactions.

(iii) At least $1,000,000 equipment leasing receipts

During the year, the qualified leasing members in the aggregate had at least $1,000,000 in gross receipts from equipment leasing.

The term ''qualified leasing group'' does not include any controlled group of corporations to which, without regard to this paragraph, paragraph (4) applies.

(C) Qualified leasing member

For purposes of this paragraph, a corporation shall be treated as a qualified leasing member for the taxable year only if for each of the taxable years referred to in subparagraph (B)—

(i) it is a component member of the controlled group of corporations, and

(ii) it meets the requirements of paragraph (4)(B) (as modified by subparagraph (A)(i) of this paragraph).

(6) Definitions relating to paragraphs (4) and (5)

For purposes of paragraphs (4) and (5)—

(A) Equipment leasing

The term ''equipment leasing'' means—

(i) the leasing of equipment which is section 1245 property, and

(ii) the purchasing, servicing, and selling of such equipment.

(B) Leasing of master sound recordings, etc., excluded

The term ''equipment leasing'' does not include the leasing of master sound recordings, and other similar contractual arrangements with respect to tangible or intangible assets associated with literary, artistic, or musical properties.

(C) Controlled group of corporations; component member

The terms ''controlled group of corporations'' and ''component member'' have the same meanings as when used in section 1563. The determination of the taxable years taken into account with respect to any controlled group of corporations shall be made in a manner consistent with the manner set forth in section 1563.

(7) Exclusion of active businesses of qualified C corporations

(A) In general

In the case of a taxpayer which is a qualified C corporation—

(i) each qualifying business carried on by such taxpayer shall be treated as a separate activity, and

(ii) subsection (a) shall not apply to losses from such business.

(B) Qualified C corporation

For purposes of subparagraph (A), the term ''qualified C corporation'' means any corporation described in subparagraph (B) of subsection (a)(1) which is not—

(i) a personal holding company (as defined in section 542(a)), or

(ii) a personal service corporation (as defined in section 269A(b) but determined by substituting ''5 percent'' for ''10 percent'' in section 269A(b)(2)).

(C) Qualifying business

For purposes of this paragraph, the term ''qualifying business'' means any active business if—

(i) during the entire 12-month period ending on the last day of the taxable year, such corporation had at least 1 full-time employee substantially all the services of whom were in the active management of such business,

(ii) during the entire 12-month period ending on the last day of the taxable year, such corporation had at least 3 full-time, nonowner employees substantially all of the services of whom were services directly related to such business,

(iii) the amount of the deductions attributable to such business which are allowable to the taxpayer solely by reason of sections 162 and 404 for the taxable year exceeds 15 percent of the gross income from such business for such year, and

(iv) such business is not an excluded business.

(D) Special rules for application of subparagraph (C)

(i) Partnerships in which taxpayer is a qualified corporate partner

In the case of an active business of a partnership, if—

(I) the taxpayer is a qualified corporate partner in the partnership, and

(II) during the entire 12-month period ending on the last day of the partnership's taxable year, there was at least 1 full-time employee of the partnership (or of a qualified corporate partner) substantially all the services of whom were in the active management of such business,

then the taxpayer's proportionate share (determined on the basis of its profits in-

terest) of the activities of the partnership in such business shall be treated as activities of the taxpayer (and clause (i) of subparagraph (C) shall not apply in determining whether such business is a qualifying business of the taxpayer).

(ii) Qualified corporate partner

For purposes of clause (i), the term ''qualified corporate partner'' means any corporation if—

(I) such corporation is a general partner in the partnership,

(II) such corporation has an interest of 10 percent or more in the profits and losses of the partnership, and

(III) such corporation has contributed property to the partnership in an amount not less than the lesser of $500,000 or 10 percent of the net worth of the corporation.

For purposes of subclause (III), any contribution of property other than money shall be taken into account at its fair market value.

(iii) Deduction for owner employee compensation not taken into account

For purposes of clause (iii) of subparagraph (C), there shall not be taken into account any deduction in respect of compensation for personal services rendered by any employee (other than a non-owner employee) of the taxpayer or any member of such employee's family (within the meaning of section 318(a)(1)).

(iv) Special rule for banks

For purposes of clause (iii) of subparagraph (C), in the case of a bank (as defined in section 581) or a financial institution to which section 591 applies—

(I) gross income shall be determined without regard to the exclusion of interest from gross income under section 103, and

(II) in addition to the deductions described in such clause, there shall also be taken into account the amount of the deductions which are allowable for amounts paid or credited to the accounts of depositors or holders of accounts as dividends or interest on their deposits or withdrawable accounts under section 163 or 591.

(v) Special rule for life insurance companies

(I) In general

Clause (iii) of subparagraph (C) shall not apply to any insurance business of a qualified life insurance company.

(II) Insurance business

For purposes of subclause (I), the term ''insurance business'' means any business which is not a noninsurance business (within the meaning of section 453B(e)(3)).

(III) Qualified life insurance company

For purposes of subclause (I), the term ''qualified life insurance company'' means any company which would be a life insurance company as defined in section 816 if unearned premiums were not taken into account under subsections (a)(2) and (c)(2) of section 816.

(E) Definitions

For purposes of this paragraph—

(i) Non-owner employee

The term ''non-owner employee'' means any employee who does not own, at any time during the taxable year, more than 5 percent in value of the outstanding stock of the taxpayer. For purposes of the preceding sentence, section 318 shall apply, except that ''5 percent'' shall be substituted for ''50 percent'' in section 318(a)(2)(C).

(ii) Excluded business

The term ''excluded business'' means—

(I) equipment leasing (as defined in paragraph (6)), and

(II) any business involving the use, exploitation, sale, lease, or other disposition of master sound recordings, motion picture films, video tapes, or tangible or intangible assets associated with literary, artistic, musical, or similar properties.

(iii) Special rules relating to communications industry, etc.

(I) Business not excluded where taxpayer not completely at risk

A business involving the use, exploitation, sale, lease, or other disposition of property described in subclause (II) of clause (ii) shall not constitute an excluded business by reason of such subclause if the taxpayer is at risk with respect to all amounts paid or incurred (or chargeable to capital account) in such business.

(II) Certain licensed businesses not excluded

For purposes of subclause (II) of clause (ii), the provision of radio, television, cable television, or similar services pursuant to a license or franchise granted by the Federal Communications Commission or any other Federal, State, or local authority shall not constitute an excluded business by reason of such subclause.

(F) Affiliated group treated as 1 taxpayer

For purposes of this paragraph—

(i) In general

Except as provided in subparagraph (G), the component members of an affiliated group of corporations shall be treated as a single taxpayer.

(ii) Affiliated group of corporations

The term ''affiliated group of corporations'' means an affiliated group (as defined in section 1504(a)) which files or is required to file consolidated income tax returns.

(iii) Component member

The term ''component member'' means an includible corporation (as defined in section 1504) which is a member of the affiliated group.

(G) Loss of 1 member of affiliated group may not offset income of personal holding company or personal service corporation

Nothing in this paragraph shall permit any loss of a member of an affiliated group to be used as an offset against the income of any other member of such group which is a personal holding company (as defined in section 542(a)) or a personal service corporation (as defined in section 269A(b) but determined by substituting ''5 percent'' for ''10 percent'' in section 269A(b)(2)).

(d) Definition of loss

For purposes of this section, the term ''loss'' means the excess of the deductions allowable under this chapter for the taxable year (determined without regard to the first sentence of subsection (a)) and allocable to an activity to which this section applies over the income received or accrued by the taxpayer during the taxable year from such activity (determined without regard to subsection (e)(1)(A)).

(e) Recapture of losses where amount at risk is less than zero

(1) In general

If zero exceeds the amount for which the taxpayer is at risk in any activity at the close of any taxable year—

(A) the taxpayer shall include in his gross income for such taxable year (as income from such activity) an amount equal to such excess, and

(B) an amount equal to the amount so included in gross income shall be treated as a deduction allocable to such activity for the first succeeding taxable year.

(2) Limitation

The excess referred to in paragraph (1) shall not exceed—

(A) the aggregate amount of the reductions required by subsection (b)(5) with respect to the activity by reason of losses for all prior taxable years beginning after December 31, 1978, reduced by

(B) the amounts previously included in gross income with respect to such activity under this subsection.

(Added Pub. L. 94–455, title II, §204(a), Oct. 4, 1976, 90 Stat. 1531; amended Pub. L. 95–600, title II, §§201(a), (c)(1), 202, 203, title VII, §701(k)(2), Nov. 6, 1978, 92 Stat. 2814, 2816, 2906; Pub. L. 95–618, title IV, §402(d), Nov. 9, 1978, 92 Stat. 3202; Pub. L. 96–222, title I, §102(a)(1)(A)–(D), Apr. 1, 1980, 94 Stat. 206; Pub. L. 97–354, §5(a)(31), Oct. 19, 1982, 96 Stat. 1695; Pub. L. 98–369, div. A, title IV, §432(a)–(c), title VII, §721(x)(2), July 18, 1984, 98 Stat. 811–814, 971; Pub. L. 99–514, title II, §201(d)(7)(A), title V, §503(a), (b), title X, §1011(b)(1), Oct. 22, 1986, 100 Stat. 2141, 2243, 2389; Pub. L. 101–508, title XI, §§11813(b)(15), 11815(b)(3), Nov. 5, 1990, 104 Stat. 1388–555, 1388–558; Pub. L. 108–357, title IV, §413(c)(7), Oct. 22, 2004, 118 Stat. 1507; Pub. L. 113–295, div. A, title II, §221(a)(59), Dec. 19, 2014, 128 Stat. 4047; Pub. L. 115–97, title I, §13512(b)(2), Dec. 22, 2017, 131 Stat. 2143.)

AMENDMENTS

2017—Subsec. (c)(7)(D)(v)(II). Pub. L. 115–97 substituted ''section 453B(e)(3)'' for ''section 806(b)(3)''.

2014—Subsec. (c)(3)(A). Pub. L. 113–295 substituted ''This'' for ''In the case of taxable years beginning after December 31, 1978, this''.

2004—Subsec. (c)(7)(B). Pub. L. 108–357 inserted ''or'' at end of cl. (i), redesignated cl. (iii) as (ii), and struck out former cl. (ii) which read as follows: ''a foreign personal holding company (as defined in section 552(a)), or''.

1990—Subsec. (b)(6)(D). Pub. L. 101–508, §11813(b)(15), substituted ''49(a)(1)(D)(iv)'' for ''46(c)(8)(D)(iv)'' wherever appearing.

Subsec. (c)(1)(E). Pub. L. 101–508, §11815(b)(3), substituted ''section 613(e)(2)'' for ''section 613(e)(3)''.

1986—Subsec. (b)(3)(C). Pub. L. 99–514, §201(d)(7)(A), struck out ''defined'' after ''person'' in heading and amended text generally. Prior to amendment, text read as follows: ''For purposes of subparagraph (A), the term 'related person' has the meaning given such term by section 168(e)(4).''

Subsec. (b)(6). Pub. L. 99–514, §503(b), added par. (6).

Subsec. (c)(3)(D), (E). Pub. L. 99–514, §503(a), redesignated subpar. (E) as (D) and struck out former subpar. (D) which read as follows: ''In the case of activities described in subparagraph (A), the holding of real property (other than mineral property) shall be treated as a separate activity, and subsection (a) shall not apply to losses from such activity. For purposes of the preceding sentence, personal property and services which are incidental to making real property available as living accommodations shall be treated as part of the activity of holding such real property.''

Subsec. (c)(7)(D)(v)(II). Pub. L. 99–514, §1011(b)(1), substituted ''section 806(b)(3)'' for ''section 806(c)(3)''.

1984—Subsec. (a)(1)(B). Pub. L. 98–369, §721(x)(2), substituted ''a C corporation'' for ''a corporation''.

Subsec. (b)(3). Pub. L. 98–369, §432(c), designated existing provisions as subpar. (A), in subpar. (A) as so designated struck out subpar. designations ''(A)'' and ''(B)'' and substituted provisions that, except as provided by regulation, amounts borrowed shall not be considered to be at risk if such amounts are borrowed from any person who has an interest in the activity or from a related person to a person (other than the taxpayer) having such an interest for provision that such amounts would not be considered to be at risk if borrowed from a person who had an interest (other than as a creditor) in such activity or who had a relationship to the taxpayer specified in section 267(b) of this title, and added subpars. (B) and (C).

Subsec. (c)(2). Pub. L. 98–369, §432(b), designated existing provisions as subpar. (A), in subpar. (A) as so designated, redesignated former subpars. (A) to (E) as cls. (i) to (v), respectively, struck out provision that a partner's interest in a partnership or a shareholder's interest in an S corporation had to be treated as a single activity to the extent that the partnership or the S corporation was engaged in activities described in any subparagraph of this paragraph, and added subpar. (B).

Subsec. (c)(7). Pub. L. 98–369, §432(a), added par. (7).

1982—Subsec. (a)(1). Pub. L. 97–354, §5(a)(31)(A), redesignated subpar. (C) as (B). Former subpar. (B), relating to an electing small business corporation, was struck out.

Subsec. (a)(3). Pub. L. 97–354, §5(a)(31)(B), substituted ''paragraph (1)(B)'' for ''paragraph (1)(C)'' in heading and text.

Subsec. (c)(2). Pub. L. 97–354, §5(a)(31)(C), substituted ''an S corporation'' for ''an electing small business corporation'' the first place appearing and ''the S corporation'' for ''an electing small business corporation'' the second place appearing.

Subsec. (c)(3)(B)(ii). Pub. L. 97–354, § 5(a)(31)(D), substituted ''an S corporation'' for ''electing small business corporation (as defined in section 1371(b))''.

Subsec. (c)(4)(A). Pub. L. 97–354, § 5(a)(31)(E), substituted ''subsection (a)(1)(B)'' for ''subsection (a)(1)(C)''.

1980—Subsec. (a)(1)(C), (3). Pub. L. 96–222, § 102(a)(1)(A), struck out in par. (1)(C) ''(determined by reference to the rules contained in section 318 rather than under section 544)'' after ''of section 542(a)'' and added par. (3).

Subsec. (b)(5). Pub. L. 96–222, § 102(a)(1)(D)(iii), substituted ''to which subsection (a) applies'' for ''to which this section applies''.

Subsec. (c)(3)(D). Pub. L. 96–222, § 102(a)(1)(D)(ii), struck out provisions relating to equipment leasing by closely-held corporations.

Subsec. (c)(4) to (6). Pub. L. 96–222, § 102(a)(1)(D)(i), added pars. (4) to (6).

Subsec. (d). Pub. L. 96–222, § 102(a)(1)(B), inserted ''(determined without regard to subsection (e)(1)(A)'' after ''from such activity''.

Subsec. (e)(2)(A). Pub. L. 96–222, § 102(a)(1)(C), inserted ''by reason of losses'' after ''with respect to the activity''.

1978—Pub. L. 95–600, § 201(c)(1), substituted ''Deductions limited to amount at risk'' for ''Deductions limited to amount at risk in case of certain activities'' in section catchline.

Subsec. (a). Pub. L. 95–600, § 202, redesignated existing provisions as par. (1), substituted provisions relating to limitations with respect to an individual, an electing small business corporation defined under section 1371(b) of this title, and a corporation meeting the stock ownership requirements of section 542(a)(2) of this title and the rules of section 318 of this title, for provisions relating to limitations with respect to a taxpayer other than a corporation which is neither an electing small business corporation defined under section 1371(b) of this title, nor a personal holding company defined under section 542 of this title, and added par. (2).

Subsec. (c)(1)(E). Pub. L. 95–618, § 402(d)(1), added subpar. (E).

Subsec. (c)(2)(E). Pub. L. 95–618, § 402(d)(2), added subpar. (E).

Subsec. (c)(3). Pub. L. 95–600, § 201(a), added par. (3).

Subsec. (d). Pub. L. 95–600, § 701(k)(2), substituted ''(determined without regard to the first sentence of subsection (a))'' for ''(determined without regard to this section)''.

Subsec. (e). Pub. L. 95–600, § 203, added subsec. (e).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, see section 13512(c) of Pub. L. 115–97, set out as a note under section 453B of this title.

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108–357 applicable to taxable years of foreign corporations beginning after Dec. 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end, see section 413(d)(1) of Pub. L. 108–357, set out as an Effective and Termination Dates of 2004 Amendments note under section 1 of this title.

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by section 11813(b)(15) of Pub. L. 101–508 applicable to property placed in service after Dec. 31, 1990, but not applicable to any transition property (as defined in section 49(e) of this title), any property with respect to which qualified progress expenditures were previously taken into account under section 46(d) of this title, and any property described in section 46(b)(2)(C) of this title, as such sections were in effect on Nov. 4, 1990, see section 11813(c) of Pub. L. 101–508, set out as a note under section 45K of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 201(d)(7)(A) of Pub. L. 99–514 applicable to property placed in service after Dec. 31, 1986, in taxable years ending after such date, with exceptions, see sections 203 and 204 of Pub. L. 99–514, set out as a note under section 168 of this title.

Amendment by section 201(d)(7)(A) of Pub. L. 99–514 not applicable to any property placed in service before Jan. 1, 1994, if such property placed in service as part of specified rehabilitations, and not applicable to certain additional rehabilitations, see section 251(d)(2), (3) of Pub. L. 99–514, set out as a note under section 46 of this title.

Pub. L. 99–514, title V, § 503(c), Oct. 22, 1986, 100 Stat. 2244, provided that:

''(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [amending this section] shall apply to losses incurred after December 31, 1986, with respect to property placed in service by the taxpayer after December 31, 1986.

''(2) SPECIAL RULE FOR LOSSES OF S CORPORATION, PARTNERSHIP, OR PASS-THRU ENTITY.—In the case of an interest in an S corporation, a partnership, or other pass-thru entity acquired after December 31, 1986, the amendments made by this section shall apply to losses after December 31, 1986, which are attributable to property placed in service by the S corporation, partnership, or pass-thru entity on, before, or after January 1, 1986.

''(3) SPECIAL RULE FOR ATHLETIC STADIUM.—The amendments made by this section shall not apply to any losses incurred by a taxpayer with respect to the holding of a multi-use athletic stadium in Pittsburgh, Pennsylvania, which the taxpayer acquired in a sale for which a letter of understanding was entered into before April 16, 1986.''

Amendment by section 1011(b)(1) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, see section 1011(c)(1) of Pub. L. 99–514, set out as a note under section 453B of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Pub. L. 98–369, div. A, title IV, § 432(d), July 18, 1984, 98 Stat. 815, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1983; except that any loss from an activity described in section 465(c)(7)(A) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as amended by this section) which (but for the amendments made by this section) would have been treated as a deduction for the taxpayer's first taxable year beginning after December 31, 1983, under section 465(a)(2) of such Code shall be allowed as a deduction for such first taxable year notwithstanding such amendments.''

Amendment by section 721(x)(2) of Pub. L. 98–369 effective as if included in the Subchapter S Revision Act of 1982, Pub. L. 97–354, see section 721(y)(1) of Pub. L. 98–369, set out as a note under section 1361 of this title.

EFFECTIVE DATE OF 1982 AMENDMENT

Amendment by Pub. L. 97–354 applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97–354, set out as an Effective Date note under section 1361 of this title.

EFFECTIVE DATE OF 1980 AMENDMENT

Amendment by Pub. L. 96–222 effective, except as otherwise provided, as if it had been included in the provisions of the Revenue Act of 1978, Pub. L. 95–600, to which such amendment relates, see section 201 of Pub. L. 96–222, set out as a note under section 32 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Amendment by Pub. L. 95–618 applicable with respect to wells commenced on or after Oct. 1, 1978, in taxable years ending on or after such date, see section 402(e) of Pub. L. 95–618, set out as a note under section 263 of this title.

Pub. L. 95–600, title II, §204(a), Nov. 6, 1978, 92 Stat. 2817, provided that: ''The amendments made by this subtitle [amending this section and section 704 of this title and enacting provisions set out as notes under this section and section 704 of this title] shall apply to taxable years beginning after December 31, 1978.''

Pub. L. 95–600, title VII, §701(k)(3), Nov. 6, 1978, 92 Stat. 2906, provided that: ''The amendments made by this subsection [amending this section and provisions set out below] shall take effect on October 4, 1976.''

EFFECTIVE DATE AND TRANSITIONAL RULES

Pub. L. 94–455, title II, §204(c), Oct. 4, 1976, 90 Stat. 1532, as amended by Pub. L. 95–600, title VII, §701(k)(1), Nov. 6, 1978, 92 Stat. 2906; Pub. L. 99–514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(1) IN GENERAL.—Except as provided in paragraphs (2) and (3), the amendments made by this section [enacting this section] shall apply to losses attributable to amounts paid or incurred in taxable years beginning after December 31, 1975. For purposes of this subsection, any amount allowed or allowable for depreciation or amortization for any period shall be treated as an amount paid or incurred in such period.

''(2) SPECIAL TRANSITIONAL RULES FOR MOVIES AND VIDEO TAPES.—

''(A) IN GENERAL.—In the case of any activity described in section 465(c)(1)(A) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954], the amendments made by this section shall not apply to—

''(i) deductions for depreciation or amortization with respect to property the principal production of which began before September 11, 1975, and for the purchase of which there was on September 11, 1975, and at all times thereafter a binding contract, and

''(ii) deductions attributable to producing or distributing property the principal production of which began before September 11, 1975.

''(B) EXCEPTION FOR CERTAIN AGREEMENTS WHERE PRINCIPAL PHOTOGRAPHY BEGIN BEFORE 1976.—In the case of any activity described in section 465(c)(1)(A) of the Internal Revenue Code of 1986, the amendments made by this section shall not apply to deductions attributable to the producing of a film the principal photography of which began on or before December 31, 1975, if—

''(i) on September 10, 1975, there was an agreement with the director or a principal motion picture star, or on or before September 10, 1975, there had been expended (or committed to the production) an amount not less than the lower of $100,000 or 10 percent of the estimated costs of producing the film, and

''(ii) the production takes place in the United States.

Subparagraph (A) shall apply only to taxpayers who held their interests on September 10, 1975. Subparagraph (B) shall apply only to taxpayers who held their interests on December 31, 1975.

''(3) SPECIAL TRANSITIONAL RULES FOR LEASING ACTIVITIES.—

''(A) RULE FOR LEASES OTHER THAN OPERATING LEASES.—In the case of any activity described in section 465(c)(1)(C) of the Internal Revenue Code of 1986, the amendments made by this section shall not apply with respect to—

''(i) leases entered into before January 1, 1976, and

''(ii) leases where the property was ordered by the lessor or lessee before January 1, 1976.

''(B) HOLDING OF INTERESTS FOR PURPOSES OF SUBPARAGRAPH (A).—Subparagraph (A) shall apply only to taxpayers who held their interests in the property on December 31, 1975.

''(C) SPECIAL RULE FOR OPERATING LEASES.—In the case of a lease described in section 46(e)(3)(B) of the Internal Revenue Code of 1986—

''(i) subparagraph (A) shall be applied by substituting 'May 1, 1976' for 'January 1, 1976' each place it appears therein, and

''(ii) subparagraph (B) shall be applied by substituting 'April 30, 1976' for 'December 31, 1975'.''

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

TRANSITIONAL RULES FOR RECAPTURE PROVISIONS AND LEASING ACTIVITIES

Pub. L. 95–600, title II, §204(b), Nov. 6, 1978, 92 Stat. 2817, as amended by Pub. L. 96–222, title I, §102(a)(1)(E), Apr. 1, 1980, 94 Stat. 208; Pub. L. 99–514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(1) RECAPTURE PROVISIONS.—If the amount for which the taxpayer is at risk in any activity as of the close of the taxpayer's last taxable year beginning before January 1, 1979, is less than zero, section 465(e)(1) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as added by section 203 of this Act) shall be applied with respect to such activity of the taxpayer by substituting such negative amount for zero.

''(2) SPECIAL TRANSITIONAL RULES FOR LEASING ACTIVITIES.—

''(A) RULE FOR LEASES.—In the case of any activity described in section 465(c)(1)(C) of such Code in which a corporation described in section 465(a)(1)(C) of such Code is engaged, the amendments made by this subtitle [amending sections 465 and 704 of this title and enacting provisions set out as notes under sections 465 and 704 of this title] shall not apply with respect to—

''(i) leases entered into before November 1, 1978, and

''(ii) leases where the property was ordered by the lessor or lessee before November 1, 1978.

''(B) HOLDING OF INTERESTS FOR PURPOSES OF SUBPARAGRAPH (A).—Subparagraph (A) shall apply only to taxpayers who held their interests in the property on October 31, 1978.''

[§ 466. Repealed. Pub. L. 99–514, title VIII, § 823(a), Oct. 22, 1986, 100 Stat. 2373]

Section, added Pub. L. 95–600, title III, §373(a), Nov. 6, 1978, 92 Stat. 2863; amended Pub. L. 96–222, title I, §103(a)(16), Apr. 1, 1980, 94 Stat. 214, related to qualified discount coupons redeemed after close of taxable year.

EFFECTIVE DATE OF REPEAL

Pub. L. 99–514, title VIII, §823(c), Oct. 22, 1986, 100 Stat. 2374, provided:

''(1) IN GENERAL.—The amendments made by this section [amending section 461 of this title and repealing this section] shall apply to taxable years beginning after December 31, 1986.

''(2) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer who elected to have section 466 of the Internal Revenue Code of 1954 [now 1986] apply for such taxpayer's last taxable year beginning before January 1, 1987, and is required to change its method of accounting by reason of the amendments made by this section for any taxable year—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as having been made with the consent of the Secretary, and

''(C) the net amount of adjustments required by section 481 of the Internal Revenue Code of 1986 to be taken into account by the taxpayer shall—

''(i) be reduced by the balance in the suspense account under section 466(e) of such Code as of the close of such last taxable year, and

''(ii) be taken into account over a period not longer than 4 years.''

§ 467. Certain payments for the use of property or services

(a) Accrual method on present value basis

In the case of the lessor or lessee under any section 467 rental agreement, there shall be taken into account for purposes of this title for any taxable year the sum of—

(1) the amount of the rent which accrues during such taxable year as determined under subsection (b), and

(2) interest for the year on the amounts which were taken into account under this subsection for prior taxable years and which are unpaid.

(b) Accrual of rental payments

(1) Allocation follows agreement

Except as provided in paragraph (2), the determination of the amount of the rent under any section 467 rental agreement which accrues during any taxable year shall be made—

(A) by allocating rents in accordance with the agreement, and

(B) by taking into account any rent to be paid after the close of the period in an amount determined under regulations which shall be based on present value concepts.

(2) Constant rental accrual in case of certain tax avoidance transactions, etc.

In the case of any section 467 rental agreement to which this paragraph applies, the portion of the rent which accrues during any taxable year shall be that portion of the constant rental amount with respect to such agreement which is allocable to such taxable year.

(3) Agreements to which paragraph (2) applies

Paragraph (2) applies to any rental payment agreement if—

(A) such agreement is a disqualified leaseback or long-term agreement, or

(B) such agreement does not provide for the allocation referred to in paragraph (1)(A).

(4) Disqualified leaseback or long-term agreement

For purposes of this subsection, the term ''disqualified leaseback or long-term agreement'' means any section 467 rental agreement if—

(A) such agreement is part of a leaseback transaction or such agreement is for a term in excess of 75 percent of the statutory recovery period for the property, and

(B) a principal purpose for providing increasing rents under the agreement is the avoidance of tax imposed by this subtitle.

(5) Exceptions to disqualification in certain cases

The Secretary shall prescribe regulations setting forth circumstances under which agreements will not be treated as disqualified leaseback or long-term agreements, including circumstances relating to—

(A) changes in amounts paid determined by reference to price indices,

(B) rents based on a fixed percentage of lessee receipts or similar amounts,

(C) reasonable rent holidays, or

(D) changes in amounts paid to unrelated 3rd parties.

(c) Recapture of prior understated inclusions under leaseback or long-term agreements

(1) In general

If—

(A) the lessor under any section 467 rental agreement disposes of any property subject to such agreement during the term of such agreement, and

(B) such agreement is a leaseback or long-term agreement to which paragraph (2) of subsection (b) did not apply,

the recapture amount shall be treated as ordinary income. Such gain shall be recognized notwithstanding any other provision of this subtitle.

(2) Recapture amount

For purposes of paragraph (1), the term ''recapture amount'' means the lesser of—

(A) the prior understated inclusions, or

(B) the excess of the amount realized (or in the case of a disposition other than a sale, exchange, or involuntary conversion, the fair market value of the property) over the adjusted basis of such property.

The amount determined under subparagraph (B) shall be reduced by the amount of any gain treated as ordinary income on the disposition under any other provision of this subtitle.

(3) Prior understated inclusions

For purposes of this subsection, the term ''prior understated inclusion'' means the excess (if any) of—

(A) the amount which would have been taken into account by the lessor under subsection (a) for periods before the disposition if subsection (b)(2) had applied to the agreement, over

(B) the amount taken into account under subsection (a) by the lessor for periods before the disposition.

(4) Leaseback or long-term agreement

For purposes of this subsection, the term ''leaseback or long-term agreement'' means any agreement described in subsection (b)(4)(A).

(5) Special rules

Under regulations prescribed by the Secretary—

(A) exceptions similar to the exceptions applicable under section 1245 or 1250 (whichever is appropriate) shall apply for purposes of this subsection,

(B) any transferee in a disposition excepted by reason of subparagraph (A) who has a transferred basis in the property shall be treated in the same manner as the transferor, and

(C) for purposes of sections 170(e) and 751(c), amounts treated as ordinary income under this section shall be treated in the same manner as amounts treated as ordinary income under section 1245 or 1250.

(d) Section 467 rental agreements

(1) In general

Except as otherwise provided in this subsection, the term ''section 467 rental agreements'' means any rental agreement for the use of tangible property under which—

(A) there is at least one amount allocable to the use of property during a calendar year which is to be paid after the close of the calendar year following the calendar year in which such use occurs, or

(B) there are increases in the amount to be paid as rent under the agreement.

(2) Section not to apply to agreements involving payments of $250,000 or less

This section shall not apply to any amount to be paid for the use of property if the sum of the following amounts does not exceed $250,000—

(A) the aggregate amount of payments received as consideration for such use of property, and

(B) the aggregate value of any other consideration to be received for such use of property.

For purposes of the preceding sentence, rules similar to the rules of clauses (ii) and (iii) of section 1274(c)(4)(C) shall apply.

(e) Definitions

For purposes of this section—

(1) Constant rental amount

The term ''constant rental amount'' means, with respect to any section 467 rental agreement, the amount which, if paid as of the close of each lease period under the agreement, would result in an aggregate present value equal to the present value of the aggregate payments required under the agreement.

(2) Leaseback transaction

A transaction is a leaseback transaction if it involves a leaseback to any person who had an interest in such property at any time within 2 years before such leaseback (or to a related person).

(3) Statutory recovery period

(A) In general

In the case of:	The statutory recovery period is:
3-year property	3 years
5-year property	5 years
7-year property	7 years
10-year property	10 years
15-year and 20-year property	15 years
Residential rental property and nonresidential real property	19 years
Any railroad grading or tunnel bore	50 years.

(B) Special rule for property not depreciable under section 168

In the case of property to which section 168 does not apply, subparagraph (A) shall be applied as if section 168 applies to such property.

(4) Discount and interest rate

For purposes of computing present value and interest under subsection (a)(2), the rate used shall be equal to 110 percent of the applicable Federal rate determined under section 1274(d) (compounded semiannually) which is in effect at the time the agreement is entered into with respect to debt instruments having a maturity equal to the term of the agreement.

(5) Related person

The term ''related person'' has the meaning given to such term by section 465(b)(3)(C).

(6) Certain options of lessee to renew not taken into account

Except as provided in regulations prescribed by the Secretary, there shall not be taken into account in computing the term of any agreement for purposes of this section any extension which is solely at the option of the lessee.

(f) Comparable rules where agreement for decreasing payments

Under regulations prescribed by the Secretary, rules comparable to the rules of this section shall also apply in the case of any agreement where the amount paid under the agreement for the use of property decreases during the term of the agreement.

(g) Comparable rules for services

Under regulations prescribed by the Secretary, rules comparable to the rules of subsection (a)(2) shall also apply in the case of payments for services which meet requirements comparable to the requirements of subsection (d). The preceding sentence shall not apply to any amount to which section 404 or 404A (or any other provision specified in regulations) applies.

(h) Regulations

The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this section, including regulations providing for the application of this section in the case of contingent payments.

(Added Pub. L. 98–369, div. A, title I, § 92(a), July 18, 1984, 98 Stat. 609; amended Pub. L. 99–514, title II, § 201(d)(8), title V, § 511(d)(2)(A), title VI, § 631(e)(10), title XVIII, §§ 1807(b), 1879(f)(1), Oct. 22, 1986, 100 Stat. 2141, 2248, 2274, 2816, 2906; Pub. L. 100–647, title I, §§ 1002(i)(2)(H), 1005(c)(10), Nov. 10, 1988, 102 Stat. 3371, 3392; Pub. L. 108–27, title III, § 302(e)(4)(B)(ii), May 28, 2003, 117 Stat. 764.)

AMENDMENTS

2003—Subsec. (c)(5)(C). Pub. L. 108–27 struck out '', 341(e)(12),'' after ''170(e)''.

1988—Subsec. (c)(5)(C). Pub. L. 100–647, § 1005(c)(10), made technical correction to directory language of Pub. L. 99–514, § 511(d)(2)(A). See 1986 Amendment note below.

Subsec. (e)(3)(A). Pub. L. 100–647, § 1002(i)(2)(H), at end of table inserted item relating to any railroad grading or tunnel bore.

1986—Subsec. (b)(4)(A). Pub. L. 99–514, § 1807(b)(2)(A), substituted ''statutory recovery period'' for ''statutory recover period''.

Subsec. (c)(4). Pub. L. 99–514, § 1807(b)(2)(B), substituted ''subsection (b)(4)(A)'' for ''subsection (b)(3)(A)''.

Subsec. (c)(5)(C). Pub. L. 99–514, § 631(e)(10), struck out ''453B(d)(2),'' after ''341(e)(12),''.

Pub. L. 99–514, § 511(d)(2)(A), as amended by Pub. L. 100–647, § 1005(c)(10), struck out ''163(d),'' after ''sections''.

Subsec. (d)(2). Pub. L. 99–514, § 1807(b)(2)(C), substituted ''section 1274(c)(4)(C)'' for ''section 1274(c)(2)(C)''.

Subsec. (e)(3)(A). Pub. L. 99–514, § 201(d)(8)(A), in amending subpar. (A) generally, included in table 7-year property, 15-year and 20-year property, and residential rental property and nonresidential real property having recovery periods of 7, 15, and 19 years, respectively, and struck out from table low-income housing, 15-year public utility property, and 19-year real property having recovery periods of 15, 15, and 19 years, respectively.

Pub. L. 99–514, § 1879(f)(1), substituted ''19-year real property'' and ''19 years'' for ''18-year real property'' and ''18 years'', respectively.

Subsec. (e)(3)(B). Pub. L. 99–514, § 201(d)(8)(A), in amending subpar. (B) generally, substituted in heading ''not depreciable under section 168'' for ''which is not recovery property'' and in text ''In the case of property to which section 168 does not apply, subparagraph (A) shall be applied as if section 168 applies to such property.'' for ''In the case of any property, which is not recovery property, subparagraph (A) shall be applied as if such property were recovery property.''

Subsec. (e)(5). Pub. L. 99–514, § 201(d)(8)(B), substituted ''section 465(b)(3)(C)'' for ''section 168(e)(4)(D)''.

Pub. L. 99–514, § 1807(b)(2)(D), substituted ''section 168(e)(4)(D)'' for ''section 168(d)(4)(D)''.

Subsec. (g). Pub. L. 99–514, § 1807(b)(1), inserted at end ''The preceding sentence shall not apply to any amount to which section 404 or 404A (or any other provision specified in regulations) applies.''

EFFECTIVE DATE OF 2003 AMENDMENT

Amendment by Pub. L. 108–27 applicable, except as otherwise provided, to taxable years beginning after Dec. 31, 2002, see section 302(f) of Pub. L. 108–27, set out as an Effective and Termination Dates of 2003 Amendment note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 201(d)(8) of Pub. L. 99–514 applicable to property placed in service after Dec. 31, 1986, in taxable years ending after such date, with exceptions, see sections 203 and 204 of Pub. L. 99–514, set out as a note under section 168 of this title.

Amendment by section 201(d)(8) of Pub. L. 99–514 not applicable to any property placed in service before Jan. 1, 1994, if such property placed in service as part of specified rehabilitations, and not applicable to certain additional rehabilitations, see section 251(d)(2), (3) of Pub. L. 99–514, set out as a note under section 46 of this title.

Amendment by section 511(d)(2)(A) of Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, see section 511(e) of Pub. L. 99–514, set out as a note under section 163 of this title.

Amendment by section 631(e)(10) of Pub. L. 99–514 applicable to any distribution in complete liquidation, and any sale or exchange, made by a corporation after July 31, 1986, unless such corporation is completely liquidated before Jan. 1, 1987, any transaction described in section 338 of this title for which the acquisition date occurs after Dec. 31, 1986, and any distribution, not in complete liquidation, made after Dec. 31, 1986, with exceptions and special and transitional rules, see section 633 of Pub. L. 99–514, set out as an Effective Date note under section 336 of this title.

Amendment by section 1807(b) of Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

Pub. L. 99–514, title XVIII, § 1879(f)(2), Oct. 22, 1986, 100 Stat. 2906, provided that: ''The amendments made by paragraph (1) [amending this section] shall take effect as if included in the amendments made by section 103 of Public Law 99–121.''

EFFECTIVE DATE

Pub. L. 98–369, div. A, title I, § 92(c), July 18, 1984, 98 Stat. 612, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting this section] shall apply with respect to agreements entered into after June 8, 1984.

''(2) EXCEPTIONS.—The amendments made by this section shall not apply—

''(A) to any agreement entered into pursuant to a written agreement which was binding on June 8, 1984, and at all times thereafter,

''(B) subject to the provisions of paragraph (3), to any agreement to lease property if—

''(i) there was in effect a firm plan, evidenced by a board of directors' resolution, memorandum of agreement, or letter of intent on March 15, 1984, to enter into such an agreement, and

''(ii) construction of the property was commenced (but such property was not placed in service) on or before March 15, 1984, and

''(C) to any agreement to lease property if—

''(i) the lessee of such property adopted a firm plan to lease the property, evidenced by a resolution of the Finance Committee of the Board of Directors of such lessee, on February 10, 1984,

''(ii) the sum of the present values of the rents payable by the lessee under the lease at the inception thereof equals at least $91,223,034, assuming for purposes of this clause—

''(I) the annual discount rate is 12.6 percent,

''(II) the initial payment of rent occurs 12 months after the commencement of the lease, and

''(III) subsequent payments of rents occur on the anniversary date of the initial payment, and

''(iii) during—

''(I) the first 5 years of the lease, at least 9 percent of the rents payable by the lessee under the agreement are paid, and

''(II) the second 5 years of the lease, at least 16.25 percent of the rents payable by the lessee under the agreement are paid.

Paragraph (3)(B)(ii)(II) shall apply for purposes of clauses (ii) and (iii) of subparagraph (C), as if, as of the beginning of the last stage, the separate agreements were treated as 1 single agreement relating to all property covered by the agreements, including any property placed in service before the property to which the agreement for the last stage relates. If the lessor under the agreement described in subparagraph (C) leases the property from another person, this exception shall also apply to any agreement between the lessor and such person which is integrally related to, and entered into at the same time as, such agreement, and which calls for comparable payments of rent over the primary term of the agreement.

''(3) SCHEDULE OF DEEMED RENTAL PAYMENTS.—

''(A) IN GENERAL.—In any case to which paragraph (2)(B) applies, for purposes of the Internal Revenue Code of 1986 [formerly I.R.C. 1954], the lessor shall be treated as having received or accrued (and the lessee shall be treated as having paid or incurred) rents equal to the greater of—

''(i) the amount of rents actually paid under the agreement during the taxable year, or

''(ii) the amount of rents determined in accordance with the schedule under subparagraph (B) for such taxable year.

''(B) SCHEDULE.—

''(i) IN GENERAL.—The schedule under this subparagraph is as follows:

"Portion of lease term:	Cumulative percentage of total rent deemed paid:
1st ⅕	10
2nd ⅕	25
3rd ⅕	45
4th ⅕	70
Last ⅕	100.

''(ii) OPERATING RULES.—For purposes of this schedule—

''(I) the rent allocable to each taxable year within any portion of a lease term described in such schedule shall be a level pro rata amount properly allocable to such taxable year, and

''(II) any agreement relating to property which is to be placed in service in 2 or more stages shall be treated as 2 or more separate agreements.

''(C) PARAGRAPH NOT TO APPLY.—This paragraph shall not apply to any agreement if the sum of the present values of all payments under the agreement is greater than the sum of the present value of all the payments deemed to be paid or received under the schedule under subparagraph (B). For purposes of computing any present value under this subparagraph, the annual discount rate shall be equal to 12 percent, compounded semiannually.''

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

§ 468. Special rules for mining and solid waste reclamation and closing costs

(a) Establishment of reserves for reclamation and closing costs

(1) Allowance of deduction

If a taxpayer elects the application of this section with respect to any mining or solid waste disposal property, the amount of any deduction for qualified reclamation or closing costs for any taxable year to which such election applies shall be equal to the current reclamation or closing costs allocable to—

(A) in the case of qualified reclamation costs, the portion of the reserve property which was disturbed during such taxable year, and

(B) in the case of qualified closing costs, the production from the reserve property during such taxable year.

(2) Opening balance and adjustments to reserve

(A) Opening balance

The opening balance of any reserve for its first taxable year shall be zero.

(B) Increase for interest

A reserve shall be increased each taxable year by an amount equal to the amount of interest which would have been earned during such taxable year on the opening balance of such reserve for such taxable year if such interest were computed—

(i) at the Federal short-term rate or rates (determined under section 1274) in effect, and

(ii) by compounding semiannually.

(C) Reserve to be charged for amounts paid

Any amount paid by the taxpayer during any taxable year for qualified reclamation or closing costs allocable to portions of the reserve property for which the election under paragraph (1) was in effect shall be charged to the appropriate reserve as of the close of the taxable year.

(D) Reserve increased by amount deducted

A reserve shall be increased each taxable year by the amount allowable as a deduction under paragraph (1) for such taxable year which is allocable to such reserve.

(3) Allowance of deduction for excess amounts paid

There shall be allowed as a deduction for any taxable year the excess of—

(A) the amounts described in paragraph (2)(C) paid during such taxable year, over

(B) the closing balance of the reserve for such taxable year (determined without regard to paragraph (2)(C)).

(4) Limitation on balance as of the close of any taxable year

(A) Reclamation reserves

In the case of any reserve for qualified reclamation costs, there shall be included in gross income for any taxable year an amount equal to the excess of—

(i) the closing balance of the reserve for such taxable year, over

(ii) the current reclamation costs of the taxpayer for all portions of the reserve property disturbed during any taxable year to which the election under paragraph (1) applies.

(B) Closing costs reserves

In the case of any reserve for qualified closing costs, there shall be included in gross income for any taxable year an amount equal to the excess of—

(i) the closing balance of the reserve for such taxable year, over

(ii) the current closing cost of the taxpayer with respect to the reserve property, determined as if all production with respect to the reserve property for any taxable year to which the election under paragraph (1) applies had occurred in such taxable year.

(C) Order of application

This paragraph shall be applied after all adjustments to the reserve have been made for the taxable year.

(5) Income inclusions on completion or disposition

Proper inclusion in income shall be made upon—

(A) the revocation of an election under paragraph (1), or

(B) completion of the closing, or disposition of any portion, of a reserve property.

(b) Allocation for property where election not in effect for all taxable years

If the election under subsection (a)(1) is not in effect for 1 or more taxable years in which the reserved property is disturbed (or production occurs), items with respect to the reserve property shall be allocated to the reserve in such manner as the Secretary may prescribe by regulations.

(c) Revocation of election; separate reserves

(1) Revocation of election

(A) In general

The taxpayer may revoke an election under subsection (a)(1) with respect to any property. Such revocation, once made, shall be irrevocable.

(B) Time and manner of revocation

Any revocation under subparagraph (A) shall be made at such time and in such manner as the Secretary may prescribe.

(2) Separate reserves required

If a taxpayer makes an election under subsection (a)(1), the taxpayer shall establish with respect to the property for which the election was made—

(A) a separate reserve for qualified reclamation costs, and

(B) a separate reserve for qualified closing costs.

(d) Definitions and special rules relating to reclamation and closing costs

For purposes of this section—

(1) Current reclamation and closing costs

(A) Current reclamation costs

The term ''current reclamation costs'' means the amount which the taxpayer would be required to pay for qualified reclamation costs if the reclamation activities were performed currently.

(B) Current closing costs

(i) In general

The term ''current closing costs'' means the amount which the taxpayer would be required to pay for qualified closing costs if the closing activities were performed currently.

(ii) Costs computed on unit-of-production or capacity method

Estimated closing costs shall—

(I) in the case of the closing of any mine site, be computed on the unit-of-production method of accounting, and

(II) in the case of the closing of any solid waste disposal site, be computed on the unit-of-capacity method.

(2) Qualified reclamation or closing costs

The term ''qualified reclamation or closing costs'' means any of the following expenses:

(A) Mining reclamation and closing costs

Any expenses incurred for any land reclamation or closing activity which is conducted in accordance with a reclamation plan (including an amendment or modification thereof)—

(i) which—

(I) is submitted pursuant to the provisions of section 511 or 528 of the Surface Mining Control and Reclamation Act of 1977 (as in effect on January 1, 1984), and

(II) is part of a surface mining and reclamation permit granted under the provisions of title V of such Act (as so in effect), or

(ii) which is submitted pursuant to any other Federal or State law which imposes surface mining reclamation and permit requirements substantially similar to the requirements imposed by title V of such Act (as so in effect).

(B) Solid waste disposal and closing costs

(i) In general

Any expenses incurred for any land reclamation or closing activity in connection with any solid waste disposal site which is conducted in accordance with any permit issued pursuant to—

(I) any provision of the Solid Waste Disposal Act (as in effect on January 1, 1984) requiring such activity, or

(II) any other Federal, State, or local law which imposes requirements substantially similar to the requirements imposed by the Solid Waste Disposal Act (as so in effect).

(ii) Exception for certain hazardous waste sites

Clause (i) shall not apply to that portion of any property which is disturbed after the property is listed in the national contingency plan established under section 105 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980.

(3) Property

The term ''property'' has the meaning given such term by section 614.

(4) Reserve property

The term ''reserve property'' means any property with respect to which a reserve is established under subsection (a)(1).

(Added Pub. L. 98–369, div. A, title I, §91(b)(1), July 18, 1984, 98 Stat. 601; amended Pub. L. 99–514, title XVIII, §§1807(a)(3)(A), (C), 1899A(14), Oct. 22, 1986, 100 Stat. 2811, 2959; Pub. L. 101–508, title XI, §11802(c), Nov. 5, 1990, 104 Stat. 1388–529.)

REFERENCES IN TEXT

The Surface Mining Control and Reclamation Act of 1977, referred to in subsec. (d)(2)(A), is Pub. L. 95–87, Aug. 3, 1977, 91 Stat. 445, as amended. Title V of that Act is classified generally to subchapter V (§1251 et seq.) of chapter 25 of Title 30, Mineral Lands and Mining. Sections 511 and 528 of that Act are classified to sections 1261 and 1278, respectively, of Title 30. For complete classification of this Act to the Code, see Short Title note set out under section 1201 of Title 30 and Tables.

The Solid Waste Disposal Act, referred to in subsec. (d)(2)(B)(i), is title II of Pub. L. 89–272, Oct. 20, 1965, 79 Stat. 997, as amended generally by Pub. L. 94–580, §2, Oct. 21, 1976, 90 Stat. 2795, which is classified generally

to chapter 82 (§ 6901 et seq.) of Title 42, The Public Health and Welfare. For complete classification of this Act to the Code, see Short Title note set out under section 6901 of Title 42 and Tables.

Section 105 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, referred to in subsec. (d)(2)(B)(ii), is classified to section 9605 of Title 42.

AMENDMENTS

1990—Subsec. (a)(2)(B). Pub. L. 101–508 amended subpar. (B) generally, substituting present provisions for provisions providing for increase for interest and a phase-in of interest rates for taxable years ending before 1987.

1986—Subsec. (a)(1). Pub. L. 99–514, § 1807(a)(3)(C), substituted ''this section'' for ''this subsection''.

Subsec. (a)(2)(D). Pub. L. 99–514, § 1807(a)(3)(A), added subpar. (D).

Subsec. (d)(2)(B)(ii). Pub. L. 99–514, § 1899A(14), substituted ''Comprehensive Environmental Response, Compensation, and Liability Act of 1980'' for ''Comprehensive Environmental, Compensation, and Liability Act of 1980''.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 1807(a)(3)(A), (C) of Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE

Section effective July 18, 1984, with respect to taxable years ending after such date, except as otherwise provided, see section 91(g)(4) of Pub. L. 98–369, as amended, set out as an Effective Date of 1984 Amendment note under section 461 of this title.

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

§ 468A. Special rules for nuclear decommissioning costs

(a) In general

If the taxpayer elects the application of this section, there shall be allowed as a deduction for any taxable year the amount of payments made by the taxpayer to a Nuclear Decommissioning Reserve Fund (hereinafter referred to as the ''Fund'') during such taxable year.

(b) Limitation on amounts paid into Fund

The amount which a taxpayer may pay into the Fund for any taxable year shall not exceed the ruling amount applicable to such taxable year.

(c) Income and deductions of the taxpayer

(1) Inclusion of amounts distributed

There shall be includible in the gross income of the taxpayer for any taxable year—

(A) any amount distributed from the Fund during such taxable year, other than any amount distributed to pay costs described in subsection (e)(4)(B), and

(B) except to the extent provided in regulations, amounts properly includible in gross income in the case of any deemed distribution under subsection (e)(6), any termination under subsection (e)(7), or the disposition of any interest in the nuclear powerplant.

(2) Deduction when economic performance occurs

In addition to any deduction under subsection (a), there shall be allowable as a deduction for any taxable year the amount of the nuclear decommissioning costs with respect to which economic performance (within the meaning of section 461(h)(2)) occurs during such taxable year.

(d) Ruling amount

For purposes of this section—

(1) Request required

No deduction shall be allowed for any payment to the Fund unless the taxpayer requests, and receives, from the Secretary a schedule of ruling amounts. For purposes of the preceding sentence, the taxpayer shall request a schedule of ruling amounts upon each renewal of the operating license of the nuclear powerplant.

(2) Ruling amount

The term ''ruling amount'' means, with respect to any taxable year, the amount which the Secretary determines under paragraph (1) to be necessary to—

(A) fund the total nuclear decommissioning costs with respect to such power plant over the estimated useful life of such power plant, and

(B) prevent any excessive funding of such costs or the funding of such costs at a rate more rapid than level funding, taking into account such discount rates as the Secretary deems appropriate.

(3) Review of amount

The Secretary shall at least once during the useful life of the nuclear powerplant (or, more frequently, upon the request of the taxpayer) review, and revise if necessary, the schedule of ruling amounts determined under paragraph (1).

(e) Nuclear Decommissioning Reserve Fund

(1) In general

Each taxpayer who elects the application of this section shall establish a Nuclear Decommissioning Reserve Fund with respect to each nuclear powerplant to which such election applies.

(2) Taxation of Fund

(A) In general

There is hereby imposed on the gross income of the Fund for any taxable year a tax at the rate of 20 percent, except that—

(i) there shall not be included in the gross income of the Fund any payment to the Fund with respect to which a deduction is allowable under subsection (a), and

(ii) there shall be allowed as a deduction to the Fund any amount paid by the Fund which is described in paragraph (4)(B) (other than an amount paid to the taxpayer) and which would be deductible under this chapter for purposes of determining the taxable income of a corporation.

(B) Tax in lieu of other taxation

The tax imposed by subparagraph (A) shall be in lieu of any other taxation under this subtitle of the income from assets in the Fund.

(C) Fund treated as corporation

For purposes of subtitle F—

(i) the Fund shall be treated as if it were a corporation, and

(ii) any tax imposed by this paragraph shall be treated as a tax imposed by section 11.

(3) Contributions to Fund

Except as provided in subsection (f), the Fund shall not accept any payments (or other amounts) other than payments with respect to which a deduction is allowable under subsection (a).

(4) Use of Fund

The Fund shall be used exclusively for—

(A) satisfying, in whole or in part, any liability of any person contributing to the Fund for the decommissioning of a nuclear powerplant (or unit thereof),

(B) to pay administrative costs (including taxes) and other incidental expenses of the Fund (including legal, accounting, actuarial, and trustee expenses) in connection with the operation of the Fund, and

(C) to the extent that a portion of the Fund is not currently needed for purposes described in subparagraph (A) or (B), making investments.

(5) Prohibitions against self-dealing

Under regulations prescribed by the Secretary, for purposes of section 4951 (and so much of this title as relates to such section), the Fund shall be treated in the same manner as a trust described in section 501(c)(21).

(6) Disqualification of Fund

In any case in which the Fund violates any provision of this section or section 4951, the Secretary may disqualify such Fund from the application of this section. In any case to which this paragraph applies, the Fund shall be treated as having distributed all of its funds on the date such determination takes effect.

(7) Termination upon completion

Upon substantial completion of the nuclear decommissioning of the nuclear powerplant with respect to which a Fund relates, the taxpayer shall terminate such Fund.

(f) Transfers into qualified funds

(1) In general

Notwithstanding subsection (b), any taxpayer maintaining a Fund to which this section applies with respect to a nuclear power plant may transfer into such Fund not more than an amount equal to the present value of the portion of the total nuclear decommissioning costs with respect to such nuclear power plant previously excluded for such nuclear power plant under subsection (d)(2)(A) as in effect immediately before the date of the enactment of this subsection.

(2) Deduction for amounts transferred

(A) In general

Except as provided in subparagraph (C), the deduction allowed by subsection (a) for any transfer permitted by this subsection shall be allowed ratably over the remaining estimated useful life (within the meaning of subsection (d)(2)(A)) of the nuclear power plant beginning with the taxable year during which the transfer is made.

(B) Denial of deduction for previously deducted amounts

No deduction shall be allowed for any transfer under this subsection of an amount for which a deduction was previously allowed to the taxpayer (or a predecessor) or a corresponding amount was not included in gross income of the taxpayer (or a predecessor). For purposes of the preceding sentence, a ratable portion of each transfer shall be treated as being from previously deducted or excluded amounts to the extent thereof.

(C) Transfers of qualified funds

If—

(i) any transfer permitted by this subsection is made to any Fund to which this section applies, and

(ii) such Fund is transferred thereafter,

any deduction under this subsection for taxable years ending after the date that such Fund is transferred shall be allowed to the transferor for the taxable year which includes such date.

(D) Special rules

(i) Gain or loss not recognized on transfers to Fund

No gain or loss shall be recognized on any transfer described in paragraph (1).

(ii) Transfers of appreciated property to Fund

If appreciated property is transferred in a transfer described in paragraph (1), the amount of the deduction shall not exceed the adjusted basis of such property.

(3) New ruling amount required

Paragraph (1) shall not apply to any transfer unless the taxpayer requests from the Secretary a new schedule of ruling amounts in connection with such transfer.

(4) No basis in qualified funds

Notwithstanding any other provision of law, the taxpayer's basis in any Fund to which this

section applies shall not be increased by reason of any transfer permitted by this subsection.

(g) Nuclear powerplant

For purposes of this section, the term ''nuclear powerplant'' includes any unit thereof.

(h) Time when payments deemed made

For purposes of this section, a taxpayer shall be deemed to have made a payment to the Fund on the last day of a taxable year if such payment is made on account of such taxable year and is made within 2½ months after the close of such taxable year.

(Added Pub. L. 98–369, div. A, title I, § 91(c)(1), July 18, 1984, 98 Stat. 604; amended Pub. L. 99–514, title XVIII, § 1807(a)(4)(A)(i), (B)–(E)(vi), Oct. 22, 1986, 100 Stat. 2812, 2813; Pub. L. 102–486, title XIX, § 1917(a), (b), Oct. 24, 1992, 106 Stat. 3024, 3025; Pub. L. 104–188, title I, § 1704(j)(6), Aug. 20, 1996, 110 Stat. 1882; Pub. L. 109–58, title XIII, § 1310(a)–(e), Aug. 8, 2005, 119 Stat. 1007–1009.)

REFERENCES IN TEXT

The date of the enactment of this subsection, referred to in subsec. (f)(1), is the date of enactment of Pub. L. 109–58, which was approved Aug. 8, 2005.

AMENDMENTS

2005—Subsec. (b). Pub. L. 109–58, § 1310(a), reenacted heading without change and amended text of subsec. (b) generally. Prior to amendment, text read as follows: ''The amount which a taxpayer may pay into the Fund for any taxable year shall not exceed the lesser of—

''(1) the amount of nuclear decommissioning costs allocable to the Fund which is included in the taxpayer's cost of service for ratemaking purposes for such taxable year, or

''(2) the ruling amount applicable to such taxable year.''

Subsec. (d)(1). Pub. L. 109–58, § 1310(c), inserted at end ''For purposes of the preceding sentence, the taxpayer shall request a schedule of ruling amounts upon each renewal of the operating license of the nuclear powerplant.''

Subsec. (d)(2)(A). Pub. L. 109–58, § 1310(b)(2), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''fund that portion of the nuclear decommissioning costs of the taxpayer with respect to the nuclear powerplant which bears the same ratio to the total nuclear decommissioning costs with respect to such nuclear powerplant as the period for which the Fund is in effect bears to the estimated useful life of such nuclear powerplant, and''.

Subsec. (e)(2)(A). Pub. L. 109–58, § 1310(e)(1), substituted ''rate of 20 percent'' for ''rate set forth in subparagraph (B)'' in introductory provisions.

Subsec. (e)(2)(B) to (D). Pub. L. 109–58, § 1310(e)(2), (3), redesignated subpars. (C) and (D) as (B) and (C), respectively, and struck out heading and text of former subpar. (B). Text read as follows: ''For purposes of subparagraph (A), the rate set forth in this subparagraph is—

''(i) 22 percent in the case of taxable years beginning in calendar year 1994 or 1995, and

''(ii) 20 percent in the case of taxable years beginning after December 31, 1995.''

Subsec. (e)(3). Pub. L. 109–58, § 1310(d), substituted ''Except as provided in subsection (f), the Fund'' for ''The Fund''.

Subsecs. (f) to (h). Pub. L. 109–58, § 1310(b)(1), added subsec. (f) and redesignated former subsecs. (f) and (g) as (g) and (h), respectively.

1996—Subsec. (e)(2)(A). Pub. L. 104–188 provided that the amendment made by section 1917(b)(1) of Pub. L. 102–486 shall be applied as if ''at a rate'' appeared instead of ''at the rate'' in the material proposed to be stricken. See 1992 Amendment note below.

1992—Subsec. (e)(2)(A). Pub. L. 102–486, § 1917(b)(1), which directed that subpar. (A) be amended by striking ''at the rate equal to the highest rate of tax specified in section 11(b)'' and inserting ''at the rate set forth in subparagraph (B)'', was executed by making the substitution for ''at a rate equal to the highest rate of tax specified in section 11(b)''. See 1996 Amendment note above.

Subsec. (e)(2)(B) to (D). Pub. L. 102–486, § 1917(b)(2), added subpar. (B) and redesignated former subpars. (B) and (C) as (C) and (D), respectively.

Subsec. (e)(4)(C). Pub. L. 102–486, § 1917(a), struck out before period at end ''described in section 501(c)(21)(B)(ii)''.

1986—Subsec. (a). Pub. L. 99–514, § 1807(a)(4)(E)(i), substituted ''this section'' for ''this subsection''.

Subsec. (c)(1)(A). Pub. L. 99–514, § 1807(a)(4)(B), substituted ''subsection (e)(4)(B)'' for ''subsection (e)(2)(B)''.

Subsec. (d). Pub. L. 99–514, § 1807(a)(4)(E)(ii), substituted ''this section'' for ''this subsection'' in introductory text.

Subsec. (e). Pub. L. 99–514, § 1807(a)(4)(E)(iii), substituted ''Reserve Fund'' for ''Trust Fund'' in heading.

Subsec. (e)(1). Pub. L. 99–514, § 1807(a)(4)(E)(iv), substituted ''this section'' for ''this subsection'' and ''Reserve Fund'' for ''Trust Fund''.

Subsec. (e)(2). Pub. L. 99–514, § 1807(a)(4)(C), amended par. (2) generally. Prior to amendment, par. (2) read as follows: ''There is imposed on the gross income of the Fund for any taxable year a tax at a rate equal to the maximum rate in effect under section 11(b), except that—

''(A) there shall not be included in the gross income of the Fund any payment to the Fund with respect to which a deduction is allowable under subsection (a), and

''(B) there shall be allowed as a deduction any amount paid by the Fund described in paragraph (4)(B) (other than to the taxpayer).''

Subsec. (e)(4)(C). Pub. L. 99–514, § 1807(a)(4)(D), added subpar. (C).

Subsec. (e)(6). Pub. L. 99–514, § 1807(a)(4)(E)(v), substituted ''this section'' for ''this subsection'' in two places and ''this paragraph'' for ''this subparagraph''.

Subsec. (f). Pub. L. 99–514, § 1807(a)(4)(E)(vi), substituted ''For purposes of this section, the'' for ''The''.

Subsec. (g). Pub. L. 99–514, § 1807(a)(4)(A)(i), added subsec. (g).

EFFECTIVE DATE OF 2005 AMENDMENT

Pub. L. 109–58, title XIII, § 1310(f), Aug. 8, 2005, 119 Stat. 1009, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2005.''

EFFECTIVE DATE OF 1992 AMENDMENT

Pub. L. 102–486, title XIX, § 1917(c), Oct. 24, 1992, 106 Stat. 3025, provided that:

''(1) SUBSECTION (a).—The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1992.

''(2) SUBSECTION (b).—The amendments made by subsection (b) [amending this section] shall apply to taxable years beginning after December 31, 1993. Section 15 of the Internal Revenue Code of 1986 shall not apply to any change in rate resulting from the amendment made by subsection (b).''

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE

Section effective July 18, 1984, with respect to taxable years ending after such date, see section 91(g)(5) of Pub.

L. 98–369, as amended, set out as an Effective Date of 1984 Amendment note under section 461 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

TRANSITIONAL RULE

Pub. L. 99–514, title XVIII, § 1807(a)(4)(A)(ii), Oct. 22, 1986, 100 Stat. 2812, provided that: ''To the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate, subsection (g) of section 468A of the Internal Revenue Code of 1954 [now 1986] (as added by clause (i)) shall be applied with respect to any payment on account of a taxable year beginning before January 1, 1987, as if it did not contain the requirement that the payment be made within 2½ months after the close of the taxable year. Such regulations may provide that, to the extent such payment to the Fund is made more than 2½ months after the close of the taxable year, any adjustment to the tax attributable to such payment shall not affect the amount of interest payable with respect to periods before the payment is made. Such regulations may provide appropriate adjustments to the deduction allowed under such section 468A for any such taxable year to take into account the fact that the payment to the Fund is made more than 2½ months after the close of the taxable year.''

§ 468B. Special rules for designated settlement funds

(a) In general

For purposes of section 461(h), economic performance shall be deemed to occur as qualified payments are made by the taxpayer to a designated settlement fund.

(b) Taxation of designated settlement fund

(1) In general

There is imposed on the gross income of any designated settlement fund for any taxable year a tax at a rate equal to the maximum rate in effect for such taxable year under section 1(e).

(2) Certain expenses allowed

For purposes of paragraph (1), gross income for any taxable year shall be reduced by the amount of any administrative costs (including State and local taxes) and other incidental expenses of the designated settlement fund (including legal, accounting, and actuarial expenses)—

(A) which are incurred in connection with the operation of the fund, and

(B) which would be deductible under this chapter for purposes of determining the taxable income of a corporation.

No other deduction shall be allowed to the fund.

(3) Transfers to the fund

In the case of any qualified payment made to the fund—

(A) the amount of such payment shall not be treated as income of the designated settlement fund,

(B) the basis of the fund in any property which constitutes a qualified payment shall be equal to the fair market value of such property at the time of payment, and

(C) the fund shall be treated as the owner of the property in the fund (and any earnings thereon).

(4) Tax in lieu of other taxation

The tax imposed by paragraph (1) shall be in lieu of any other taxation under this subtitle of income from assets in the designated settlement fund.

(5) Coordination with subtitle F

For purposes of subtitle F—

(A) a designated settlement fund shall be treated as a corporation, and

(B) any tax imposed by this subsection shall be treated as a tax imposed by section 11.

(c) Deductions not allowed for transfer of insurance amounts

No deduction shall be allowable for any qualified payment by the taxpayer of any amounts received from the settlement of any insurance claim to the extent such amounts are excluded from the gross income of the taxpayer.

(d) Definitions

For purposes of this section—

(1) Qualified payment

The term ''qualified payment'' means any money or property which is transferred to any designated settlement fund pursuant to a court order, other than—

(A) any amount which may be transferred from the fund to the taxpayer (or any related person), or

(B) the transfer of any stock or indebtedness of the taxpayer (or any related person).

(2) Designated settlement fund

The term ''designated settlement fund'' means any fund—

(A) which is established pursuant to a court order and which extinguishes completely the taxpayer's tort liability with respect to claims described in subparagraph (D),

(B) with respect to which no amounts may be transferred other than in the form of qualified payments,

(C) which is administered by persons a majority of whom are independent of the taxpayer,

(D) which is established for the principal purpose of resolving and satisfying present and future claims against the taxpayer (or any related person or formerly related person) arising out of personal injury, death, or property damage,

(E) under the terms of which the taxpayer (or any related person) may not hold any beneficial interest in the income or corpus of the fund, and

(F) with respect to which an election is made under this section by the taxpayer.

An election under this section shall be made at such time and in such manner as the Secretary shall by regulation prescribe. Such an

election, once made, may be revoked only with the consent of the Secretary.

(3) Related person

The term ''related person'' means a person related to the taxpayer within the meaning of section 267(b).

(e) Nonapplicability of section

This section (other than subsection (g)) shall not apply with respect to any liability of the taxpayer arising under any workers' compensation Act or any contested liability of the taxpayer within the meaning of section 461(f).

(f) Other funds

Except as provided in regulations, any payment in respect of a liability described in subsection (d)(2)(D) (and not described in subsection (e)) to a trust fund or escrow fund which is not a designated settlement fund shall not be treated as constituting economic performance.

(g) Clarification of taxation of certain funds

(1) In general

Except as provided in paragraph (2), nothing in any provision of law shall be construed as providing that an escrow account, settlement fund, or similar fund is not subject to current income tax. The Secretary shall prescribe regulations providing for the taxation of any such account or fund whether as a grantor trust or otherwise.

(2) Exemption from tax for certain settlement funds

An escrow account, settlement fund, or similar fund shall be treated as beneficially owned by the United States and shall be exempt from taxation under this subtitle if—

(A) it is established pursuant to a consent decree entered by a judge of a United States District Court,

(B) it is created for the receipt of settlement payments as directed by a government entity for the sole purpose of resolving or satisfying one or more claims asserting liability under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980,

(C) the authority and control over the expenditure of funds therein (including the expenditure of contributions thereto and any net earnings thereon) is with such government entity, and

(D) upon termination, any remaining funds will be disbursed to such government entity for use in accordance with applicable law.

For purposes of this paragraph, the term ''government entity'' means the United States, any State or political subdivision thereof, the District of Columbia, any possession of the United States, and any agency or instrumentality of any of the foregoing.

(Added Pub. L. 99–514, title XVIII, § 1807(a)(7)(A), Oct. 22, 1986, 100 Stat. 2814; amended Pub. L. 100–647, title I, § 1018(f)(1), (2), (4), (5)(A), Nov. 10, 1988, 102 Stat. 3582; Pub. L. 101–508, title XI, § 11702(e)(1), Nov. 5, 1990, 104 Stat. 1388–515; Pub. L. 109–222, title II, § 201(a), May 17, 2006, 120 Stat. 347; Pub. L. 109–432, div. A, title IV, § 409(a), Dec. 20, 2006, 120 Stat. 2963.)

REFERENCES IN TEXT

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980, referred to in subsec. (g)(2)(B), is Pub. L. 96–510, Dec. 11, 1980, 94 Stat. 2767, as amended, which is classified principally to chapter 103 (§ 9601 et seq.) of Title 42, The Public Health and Welfare. For complete classification of this Act to the Code, see Short Title note set out under section 9601 of Title 42 and Tables.

AMENDMENTS

2006—Subsec. (g). Pub. L. 109–222 reenacted heading without change and amended text of subsec. (g) generally. Prior to amendment, text read as follows: ''Nothing in any provision of law shall be construed as providing that an escrow account, settlement fund, or similar fund is not subject to current income tax. The Secretary shall prescribe regulations providing for the taxation of any such account or fund whether as a grantor trust or otherwise.''

Subsec. (g)(3). Pub. L. 109–432 struck out heading and text of par. (3). Text read as follows: ''Paragraph (2) shall not apply to accounts and funds established after December 31, 2010.''

1990—Subsec. (e). Pub. L. 101–508 substituted ''This section (other than subsection (g))'' for ''This section''.

1988—Subsec. (b)(2). Pub. L. 100–647, § 1018(f)(4)(B), substituted ''No other'' for ''no other'' in concluding provisions.

Subsec. (b)(2)(B). Pub. L. 100–647, § 1018(f)(4)(A), substituted ''a corporation.'' for ''the corporation,''.

Subsec. (d)(1)(A). Pub. L. 100–647, § 1018(f)(1), inserted ''(or any related person)'' after ''taxpayer''.

Subsec. (d)(2)(A). Pub. L. 100–647, § 1018(f)(2), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''which is established pursuant to a court order,''.

Subsec. (d)(2)(E). Pub. L. 100–647, § 1018(f)(1), inserted ''(or any related person)'' after ''taxpayer''.

Subsec. (g). Pub. L. 100–647, § 1018(f)(5)(A), added subsec. (g).

EFFECTIVE DATE OF 2006 AMENDMENT

Pub. L. 109–432, div. A, title IV, § 409(b), Dec. 20, 2006, 120 Stat. 2963, provided that: ''The amendment made by this section [amending this section] shall take effect as if included in section 201 of the Tax Increase Prevention and Reconciliation Act of 2005 [Pub. L. 109–222].''

Pub. L. 109–222, title II, § 201(b), May 17, 2006, 120 Stat. 348, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to accounts and funds established after the date of the enactment of this Act [May 17, 2006].''

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101–508 effective as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 11702(j) of Pub. L. 101–508, set out as a note under section 59 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

EFFECTIVE DATE

Section effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as an Effective Date of 1986 Amendment note under section 48 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147

and 1171–1177] or title XVIII [§§1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

SPECIAL RULE FOR TAXPAYER IN BANKRUPTCY REORGANIZATION

Pub. L. 99–514, title XVIII, §1807(a)(7)(C), Oct. 22, 1986, 100 Stat. 2816, as amended by Pub. L. 100–647, title I, §1018(f)(3), Nov. 10, 1988, 102 Stat. 3582, provided that: ''In the case of any settlement fund which is established for claimants against a corporation which filed a petition for reorganization under chapter 11 of title 11, United States Code, on August 26, 1982, and which filed with a United States district court a first amended and restated plan of reorganization before March 1, 1986—

''(i) any portion of such fund which is established pursuant to a court order and with qualified payments, which meets the requirements of subparagraphs (C) and (D) of section 468B(d)(2) of the Internal Revenue Code of 1954 [now 1986] (as added by this paragraph), and with respect to which an election is made under subparagraph (F) thereof, shall be treated as a designated settlement fund for purposes of section 468B of such Code,

''(ii) such corporation (or any successor thereof) shall be liable for the tax imposed by section 468B of such Code on such portion of the fund (and the fund shall not be liable for such tax), such tax shall be deductible by the corporation, and the rate of tax under section 468B of such Code for any taxable year shall be equal to 15 percent, and

''(iii) any transaction by any portion of the fund not described in clause (i) shall be treated as a transaction made by the corporation.''

CLARIFICATION OF LAW WITH RESPECT TO CERTAIN FUNDS

Pub. L. 99–514, title XVIII, §1807(a)(7)(D), Oct. 22, 1986, 100 Stat. 2816, provided that nothing in any provision of law be construed as providing that an escrow account, settlement fund, or similar fund established after Aug. 16, 1986, not be subject to current income tax and that if contributions to such account or fund are not deductible then the account or fund be taxed as a grantor trust, prior to repeal by Pub. L. 100–647, title I, §1018(f)(5)(B), Nov. 10, 1988, 102 Stat. 3582.

§ 469. Passive activity losses and credits limited

(a) Disallowance

(1) In general

If for any taxable year the taxpayer is described in paragraph (2), neither—

(A) the passive activity loss, nor

(B) the passive activity credit,

for the taxable year shall be allowed.

(2) Persons described

The following are described in this paragraph:

(A) any individual, estate, or trust,

(B) any closely held C corporation, and

(C) any personal service corporation.

(b) Disallowed loss or credit carried to next year

Except as otherwise provided in this section, any loss or credit from an activity which is disallowed under subsection (a) shall be treated as a deduction or credit allocable to such activity in the next taxable year.

(c) Passive activity defined

For purposes of this section—

(1) In general

The term ''passive activity'' means any activity—

(A) which involves the conduct of any trade or business, and

(B) in which the taxpayer does not materially participate.

(2) Passive activity includes any rental activity

Except as provided in paragraph (7), the term ''passive activity'' includes any rental activity.

(3) Working interests in oil and gas property

(A) In general

The term ''passive activity'' shall not include any working interest in any oil or gas property which the taxpayer holds directly or through an entity which does not limit the liability of the taxpayer with respect to such interest.

(B) Income in subsequent years

If any taxpayer has any loss for any taxable year from a working interest in any oil or gas property which is treated as a loss which is not from a passive activity, then any net income from such property (or any property the basis of which is determined in whole or in part by reference to the basis of such property) for any succeeding taxable year shall be treated as income of the taxpayer which is not from a passive activity. If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income.

(4) Material participation not required for paragraphs (2) and (3)

Paragraphs (2) and (3) shall be applied without regard to whether or not the taxpayer materially participates in the activity.

(5) Trade or business includes research and experimentation activity

For purposes of paragraph (1)(A), the term ''trade or business'' includes any activity involving research or experimentation (within the meaning of section 174).

(6) Activity in connection with trade or business or production of income

To the extent provided in regulations, for purposes of paragraph (1)(A), the term ''trade or business'' includes—

(A) any activity in connection with a trade or business, or

(B) any activity with respect to which expenses are allowable as a deduction under section 212.

(7) Special rules for taxpayers in real property business

(A) In general

If this paragraph applies to any taxpayer for a taxable year—

(i) paragraph (2) shall not apply to any rental real estate activity of such taxpayer for such taxable year, and

(ii) this section shall be applied as if each interest of the taxpayer in rental real estate were a separate activity.

Notwithstanding clause (ii), a taxpayer may elect to treat all interests in rental real estate as one activity. Nothing in the preceding provisions of this subparagraph shall be construed as affecting the determination of whether the taxpayer materially participates with respect to any interest in a limited partnership as a limited partner.

(B) Taxpayers to whom paragraph applies

This paragraph shall apply to a taxpayer for a taxable year if—

(i) more than one-half of the personal services performed in trades or businesses by the taxpayer during such taxable year are performed in real property trades or businesses in which the taxpayer materially participates, and

(ii) such taxpayer performs more than 750 hours of services during the taxable year in real property trades or businesses in which the taxpayer materially participates.

In the case of a joint return, the requirements of the preceding sentence are satisfied if and only if either spouse separately satisfies such requirements. For purposes of the preceding sentence, activities in which a spouse materially participates shall be determined under subsection (h).

(C) Real property trade or business

For purposes of this paragraph, the term ''real property trade or business'' means any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business.

(D) Special rules for subparagraph (B)

(i) Closely held C corporations

In the case of a closely held C corporation, the requirements of subparagraph (B) shall be treated as met for any taxable year if more than 50 percent of the gross receipts of such corporation for such taxable year are derived from real property trades or businesses in which the corporation materially participates.

(ii) Personal services as an employee

For purposes of subparagraph (B), personal services performed as an employee shall not be treated as performed in real property trades or businesses. The preceding sentence shall not apply if such employee is a 5-percent owner (as defined in section 416(i)(1)(B)) in the employer.

(d) Passive activity loss and credit defined

For purposes of this section—

(1) Passive activity loss

The term ''passive activity loss'' means the amount (if any) by which—

(A) the aggregate losses from all passive activities for the taxable year, exceed

(B) the aggregate income from all passive activities for such year.

(2) Passive activity credit

The term ''passive activity credit'' means the amount (if any) by which—

(A) the sum of the credits from all passive activities allowable for the taxable year under—

(i) subpart D of part IV of subchapter A, or

(ii) subpart B (other than section 27) of such part IV, exceeds

(B) the regular tax liability of the taxpayer for the taxable year allocable to all passive activities.

(e) Special rules for determining income or loss from a passive activity

For purposes of this section—

(1) Certain income not treated as income from passive activity

In determining the income or loss from any activity—

(A) In general

There shall not be taken into account—

(i) any—

(I) gross income from interest, dividends, annuities, or royalties not derived in the ordinary course of a trade or business,

(II) expenses (other than interest) which are clearly and directly allocable to such gross income, and

(III) interest expense properly allocable to such gross income, and

(ii) gain or loss not derived in the ordinary course of a trade or business which is attributable to the disposition of property—

(I) producing income of a type described in clause (i), or

(II) held for investment.

For purposes of clause (ii), any interest in a passive activity shall not be treated as property held for investment.

(B) Return on working capital

For purposes of subparagraph (A), any income, gain, or loss which is attributable to an investment of working capital shall be treated as not derived in the ordinary course of a trade or business.

(2) Passive losses of certain closely held corporations may offset active income

(A) In general

If a closely held C corporation (other than a personal service corporation) has net active income for any taxable year, the passive activity loss of such taxpayer for such taxable year (determined without regard to this paragraph)—

(i) shall be allowable as a deduction against net active income, and

(ii) shall not be taken into account under subsection (a) to the extent so allowable as a deduction.

A similar rule shall apply in the case of any passive activity credit of the taxpayer.

(B) Net active income

For purposes of this paragraph, the term ''net active income'' means the taxable income of the taxpayer for the taxable year determined without regard to—

(i) any income or loss from a passive activity, and

(ii) any item of gross income, expense, gain, or loss described in paragraph (1)(A).

(3) Compensation for personal services

Earned income (within the meaning of section 911(d)(2)(A)) shall not be taken into account in computing the income or loss from a passive activity for any taxable year.

(4) Dividends reduced by dividends received deduction

For purposes of paragraphs (1) and (2), income from dividends shall be reduced by the amount of any dividends received deduction under section 243 or 245.

(f) Treatment of former passive activities

For purposes of this section—

(1) In general

If an activity is a former passive activity for any taxable year—

(A) any unused deduction allocable to such activity under subsection (b) shall be offset against the income from such activity for the taxable year,

(B) any unused credit allocable to such activity under subsection (b) shall be offset against the regular tax liability (computed after the application of paragraph (1)) allocable to such activity for the taxable year, and

(C) any such deduction or credit remaining after the application of subparagraphs (A) and (B) shall continue to be treated as arising from a passive activity.

(2) Change in status of closely held C corporation or personal service corporation

If a taxpayer ceases for any taxable year to be a closely held C corporation or personal service corporation, this section shall continue to apply to losses and credits to which this section applied for any preceding taxable year in the same manner as if such taxpayer continued to be a closely held C corporation or personal service corporation, whichever is applicable.

(3) Former passive activity

The term ''former passive activity'' means any activity which, with respect to the taxpayer—

(A) is not a passive activity for the taxable year, but

(B) was a passive activity for any prior taxable year.

(g) Dispositions of entire interest in passive activity

If during the taxable year a taxpayer disposes of his entire interest in any passive activity (or former passive activity), the following rules shall apply:

(1) Fully taxable transaction

(A) In general

If all gain or loss realized on such disposition is recognized, the excess of—

(i) any loss from such activity for such taxable year (determined after the application of subsection (b)), over

(ii) any net income or gain for such taxable year from all other passive activities (determined after the application of subsection (b)),

shall be treated as a loss which is not from a passive activity.

(B) Subparagraph (A) not to apply to disposition involving related party

If the taxpayer and the person acquiring the interest bear a relationship to each other described in section 267(b) or section 707(b)(1), then subparagraph (A) shall not apply to any loss of the taxpayer until the taxable year in which such interest is acquired (in a transaction described in subparagraph (A)) by another person who does not bear such a relationship to the taxpayer.

(C) Income from prior years

To the extent provided in regulations, income or gain from the activity for preceding taxable years shall be taken into account under subparagraph (A)(ii) for the taxable year to the extent necessary to prevent the avoidance of this section.

(2) Disposition by death

If an interest in the activity is transferred by reason of the death of the taxpayer—

(A) paragraph (1)(A) shall apply to losses described in paragraph (1)(A) to the extent such losses are greater than the excess (if any) of—

(i) the basis of such property in the hands of the transferee, over

(ii) the adjusted basis of such property immediately before the death of the taxpayer, and

(B) any losses to the extent of the excess described in subparagraph (A) shall not be allowed as a deduction for any taxable year.

(3) Installment sale of entire interest

In the case of an installment sale of an entire interest in an activity to which section 453 applies, paragraph (1) shall apply to the portion of such losses for each taxable year which bears the same ratio to all such losses as the gain recognized on such sale during such taxable year bears to the gross profit from such sale (realized or to be realized when payment is completed).

(h) Material participation defined

For purposes of this section—

(1) In general

A taxpayer shall be treated as materially participating in an activity only if the taxpayer is involved in the operations of the activity on a basis which is—

(A) regular,

(B) continuous, and

(C) substantial.

(2) Interests in limited partnerships

Except as provided in regulations, no interest in a limited partnership as a limited part-

ner shall be treated as an interest with respect to which a taxpayer materially participates.

(3) Treatment of certain retired individuals and surviving spouses

A taxpayer shall be treated as materially participating in any farming activity for a taxable year if paragraph (4) or (5) of section 2032A(b) would cause the requirements of section 2032A(b)(1)(C)(ii) to be met with respect to real property used in such activity if such taxpayer had died during the taxable year.

(4) Certain closely held C corporations and personal service corporations

A closely held C corporation or personal service corporation shall be treated as materially participating in an activity only if—

(A) 1 or more shareholders holding stock representing more than 50 percent (by value) of the outstanding stock of such corporation materially participate in such activity, or

(B) in the case of a closely held C corporation (other than a personal service corporation), the requirements of section 465(c)(7)(C) (without regard to clause (iv)) are met with respect to such activity.

(5) Participation by spouse

In determining whether a taxpayer materially participates, the participation of the spouse of the taxpayer shall be taken into account.

(i) $25,000 offset for rental real estate activities

(1) In general

In the case of any natural person, subsection (a) shall not apply to that portion of the passive activity loss or the deduction equivalent (within the meaning of subsection (j)(5)) of the passive activity credit for any taxable year which is attributable to all rental real estate activities with respect to which such individual actively participated in such taxable year (and if any portion of such loss or credit arose in another taxable year, in such other taxable year).

(2) Dollar limitation

The aggregate amount to which paragraph (1) applies for any taxable year shall not exceed $25,000.

(3) Phase-out of exemption

(A) In general

In the case of any taxpayer, the $25,000 amount under paragraph (2) shall be reduced (but not below zero) by 50 percent of the amount by which the adjusted gross income of the taxpayer for the taxable year exceeds $100,000.

(B) Special phase-out of rehabilitation credit

In the case of any portion of the passive activity credit for any taxable year which is attributable to the rehabilitation credit determined under section 47, subparagraph (A) shall be applied by substituting ''$200,000'' for ''$100,000''.

(C) Exception for low-income housing credit

Subparagraph (A) shall not apply to any portion of the passive activity credit for any taxable year which is attributable to any credit determined under section 42.

(D) Ordering rule

Paragraph (1) shall be applied for any taxable year—

(i) first, to the passive activity loss,

(ii) second, to the portion of the passive activity credit to which subparagraph (B) and[1] (C) does not apply,

(iii) third, to the portion of such credit to which subparagraph (B) applies, and

(iv) then, to the portion of such credit to which subparagraph (C) applies.

(E) Adjusted gross income

For purposes of this paragraph, adjusted gross income shall be determined without regard to—

(i) any amount includible in gross income under section 86,

(ii) the amounts excludable from gross income under sections 135 and 137,

(iii) the amounts allowable as a deduction under sections 219, 221, and 250, and

(iv) any passive activity loss or any loss allowable by reason of subsection (c)(7).

(4) Special rule for estates

(A) In general

In the case of taxable years of an estate ending less than 2 years after the date of the death of the decedent, this subsection shall apply to all rental real estate activities with respect to which such decedent actively participated before his death.

(B) Reduction for surviving spouse's exemption

For purposes of subparagraph (A), the $25,000 amount under paragraph (2) shall be reduced by the amount of the exemption under paragraph (1) (without regard to paragraph (3)) allowable to the surviving spouse of the decedent for the taxable year ending with or within the taxable year of the estate.

(5) Married individuals filing separately

(A) In general

Except as provided in subparagraph (B), in the case of any married individual filing a separate return, this subsection shall be applied by substituting—

(i) ''$12,500'' for ''$25,000'' each place it appears,

(ii) ''$50,000'' for ''$100,000'' in paragraph (3)(A), and

(iii) ''$100,000'' for ''$200,000'' in paragraph (3)(B).

(B) Taxpayers not living apart

This subsection shall not apply to a taxpayer who—

(i) is a married individual filing a separate return for any taxable year, and

(ii) does not live apart from his spouse at all times during such taxable year.

(6) Active participation

(A) In general

An individual shall not be treated as actively participating with respect to any in-

[1] So in original. Probably should be ''or''.

terest in any rental real estate activity for any period if, at any time during such period, such interest (including any interest of the spouse of the individual) is less than 10 percent (by value) of all interests in such activity.

(B) No participation requirement for low-income housing or rehabilitation credit

Paragraphs (1) and (4)(A) shall be applied without regard to the active participation requirement in the case of—

(i) any credit determined under section 42 for any taxable year, or

(ii) any rehabilitation credit determined under section 47,[2]

(C) Interest as a limited partner

Except as provided in regulations, no interest as a limited partner in a limited partnership shall be treated as an interest with respect to which the taxpayer actively participates.

(D) Participation by spouse

In determining whether a taxpayer actively participates, the participation of the spouse of the taxpayer shall be taken into account.

(j) Other definitions and special rules

For purposes of this section—

(1) Closely held C corporation

The term ''closely held C corporation'' means any C corporation described in section 465(a)(1)(B).

(2) Personal service corporation

The term ''personal service corporation'' has the meaning given such term by section 269A(b)(1), except that section 269A(b)(2) shall be applied—

(A) by substituting ''any'' for ''more than 10 percent'', and

(B) by substituting ''any'' for ''50 percent or more in value'' in section 318(a)(2)(C).

A corporation shall not be treated as a personal service corporation unless more than 10 percent of the stock (by value) in such corporation is held by employee-owners (within the meaning of section 269A(b)(2), as modified by the preceding sentence).

(3) Regular tax liability

The term ''regular tax liability'' has the meaning given such term by section 26(b).

(4) Allocation of passive activity loss and credit

The passive activity loss and the passive activity credit (and the $25,000 amount under subsection (i)) shall be allocated to activities, and within activities, on a pro rata basis in such manner as the Secretary may prescribe.

(5) Deduction equivalent

The deduction equivalent of credits from a passive activity for any taxable year is the amount which (if allowed as a deduction) would reduce the regular tax liability for such taxable year by an amount equal to such credits.

(6) Special rule for gifts

In the case of a disposition of any interest in a passive activity by gift—

(A) the basis of such interest immediately before the transfer shall be increased by the amount of any passive activity losses allocable to such interest with respect to which a deduction has not been allowed by reason of subsection (a), and

(B) such losses shall not be allowable as a deduction for any taxable year.

(7) Qualified residence interest

The passive activity loss of a taxpayer shall be computed without regard to qualified residence interest (within the meaning of section 163(h)(3)).

(8) Rental activity

The term ''rental activity'' means any activity where payments are principally for the use of tangible property.

(9) Election to increase basis of property by amount of disallowed credit

For purposes of determining gain or loss from a disposition of any property to which subsection (g)(1) applies, the transferor may elect to increase the basis of such property immediately before the transfer by an amount equal to the portion of any unused credit allowable under this chapter which reduced the basis of such property for the taxable year in which such credit arose. If the taxpayer elects the application of this paragraph, such portion of the passive activity credit of such taxpayer shall not be allowed for any taxable year.

(10) Coordination with section 280A

If a passive activity involves the use of a dwelling unit to which section 280A(c)(5) applies for any taxable year, any income, deduction, gain, or loss allocable to such use shall not be taken into account for purposes of this section for such taxable year.

(11) Aggregation of members of affiliated groups

Except as provided in regulations, all members of an affiliated group which files a consolidated return shall be treated as 1 corporation.

(12) Special rule for distributions by estates or trusts

If any interest in a passive activity is distributed by an estate or trust—

(A) the basis of such interest immediately before such distribution shall be increased by the amount of any passive activity losses allocable to such interest, and

(B) such losses shall not be allowable as a deduction for any taxable year.

(k) Separate application of section in case of publicly traded partnerships

(1) In general

This section shall be applied separately with respect to items attributable to each publicly traded partnership (and subsection (i) shall not apply with respect to items attributable to any such partnership). The preceding sentence shall not apply to any credit determined under

[2] So in original. The comma probably should be a period.

section 42, or any rehabilitation credit determined under section 47, attributable to a publicly traded partnership to the extent the amount of any such credits exceeds the regular tax liability attributable to income from such partnership.

(2) Publicly traded partnership

For purposes of this section, the term ''publicly traded partnership'' means any partnership if—

(A) interests in such partnership are traded on an established securities market, or

(B) interests in such partnership are readily tradable on a secondary market (or the substantial equivalent thereof).

(3) Coordination with subsection (g)

For purposes of subsection (g), a taxpayer shall not be treated as having disposed of his entire interest in an activity of a publicly traded partnership until he disposes of his entire interest in such partnership.

(4) Application to regulated investment companies

For purposes of this section, a regulated investment company (as defined in section 851) holding an interest in a qualified publicly traded partnership (as defined in section 851(h)) shall be treated as a taxpayer described in subsection (a)(2) with respect to items attributable to such interest.

(*l*) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out provisions of this section, including regulations—

(1) which specify what constitutes an activity, material participation, or active participation for purposes of this section,

(2) which provide that certain items of gross income will not be taken into account in determining income or loss from any activity (and the treatment of expenses allocable to such income),

(3) requiring net income or gain from a limited partnership or other passive activity to be treated as not from a passive activity,

(4) which provide for the determination of the allocation of interest expense for purposes of this section, and

(5) which deal with changes in marital status and changes between joint returns and separate returns.

(Added Pub. L. 99–514, title V, § 501(a), Oct. 22, 1986, 100 Stat. 2233; amended Pub. L. 100–203, title X, § 10212(a), Dec. 22, 1987, 101 Stat. 1330–405; Pub. L. 100–647, title I, § 1005(a)(1)–(9), (11), (12), title II, § 2004(g), title VI, § 6009(c)(3), Nov. 10, 1988, 102 Stat. 3387–3389, 3603, 3690; Pub. L. 101–239, title VII, § 7109(a), Dec. 19, 1989, 103 Stat. 2322; Pub. L. 101–508, title XI, §§ 11704(a)(6), 11813(b)(16), Nov. 5, 1990, 104 Stat. 1388–518, 1388–555; Pub. L. 103–66, title XIII, § 13143(a), (b), Aug. 10, 1993, 107 Stat. 440, 441; Pub. L. 104–188, title I, §§ 1704(d)(1), (e)(1), 1807(c)(4), Aug. 20, 1996, 110 Stat. 1878, 1902; Pub. L. 105–277, div. J, title IV, § 4003(a)(2)(D), Oct. 21, 1998, 112 Stat. 2681–908; Pub. L. 106–554, § 1(a)(7) [title I, § 101(b)], Dec. 21, 2000, 114 Stat. 2763, 2763A–599; Pub. L. 107–16, title IV, § 431(c)(3), June 7, 2001, 115 Stat. 68; Pub. L. 107–147, title IV, § 412(a), Mar. 9, 2002, 116 Stat. 53; Pub. L. 108–357, title I, § 102(d)(5), title III, § 331(g), Oct. 22, 2004, 118 Stat. 1429, 1477; Pub. L. 113–295, div. A, title II, § 221(a)(41)(G), (60)(A), Dec. 19, 2014, 128 Stat. 4044, 4047; Pub. L. 115–97, title I, §§ 13305(b)(1), 14202(b)(3), Dec. 22, 2017, 131 Stat. 2126, 2216; Pub. L. 115–141, div. U, title IV, § 401(d)(1)(D)(ii), (5)(B)(i)–(iii), Mar. 23, 2018, 132 Stat. 1206, 1210; Pub. L. 116–260, div. EE, title I, § 104(b)(2)(H), Dec. 27, 2020, 134 Stat. 3041.)

AMENDMENTS

2020—Subsec. (i)(3)(E)(iii). Pub. L. 116–260 struck out ''222,'' after ''221,''.

2018—Subsecs. (c)(3)(B), (d)(2)(A)(ii). Pub. L. 115–141, § 401(d)(1)(D)(ii), substituted ''27'' for ''27(a)''.

Subsec. (i)(3)(C). Pub. L. 115–141, § 401(d)(5)(B)(i), redesignated subpar. (D) as (C) and struck out former subpar. (C). Prior to amendment, text of subpar. (C) read as follows: ''Subparagraph (A) shall not apply to any portion of the passive activity loss for any taxable year which is attributable to the commercial revitalization deduction under section 1400I.''

Subsec. (i)(3)(D). Pub. L. 115–141, § 401(d)(5)(B)(i), (ii), redesignated subpar. (E) as (D) and amended it generally. Prior to amendment, subpar. related to ordering rules to reflect exceptions and separate phase-outs. Former subpar. (D) redesignated (C).

Subsec. (i)(3)(E), (F). Pub. L. 115–141, § 401(d)(5)(B)(i), redesignated subpar. (F) as (E). Former subpar. (E) redesignated (D).

Subsec. (i)(6)(B). Pub. L. 115–141, § 401(d)(5)(B)(iii)(I), substituted ''or rehabilitation credit'' for '', rehabilitation credit, or commercial revitalization deduction'' in heading.

Subsec. (i)(6)(B)(iii). Pub. L. 115–141, § 401(d)(5)(B)(iii)(II)–(IV), struck out cl. (iii) which read as follows: ''any deduction under section 1400I (relating to commercial revitalization deduction).''

2017—Subsec. (i)(3)(F)(iii). Pub. L. 115–97, § 14202(b)(3), substituted ''222, and 250'' for ''and 222''.

Pub. L. 115–97, § 13305(b)(1), struck out ''199,'' after ''sections''.

2014—Subsec. (e)(4). Pub. L. 113–295, § 221(a)(41)(G), struck out '', 244,'' after ''section 243''.

Subsec. (m). Pub. L. 113–295, § 221(a)(60)(A), struck out subsec. (m) which related to a phase-in of disallowance of losses and credits for interest held before the date of enactment of the Tax Reform Act of 1986.

2004—Subsec. (i)(3)(F)(iii). Pub. L. 108–357, § 102(d)(5), inserted ''199,'' before ''219,''.

Subsec. (k)(4). Pub. L. 108–357, § 331(g), added par. (4).

2002—Subsec. (i)(3)(E)(ii) to (iv). Pub. L. 107–147 added cls. (ii) to (iv) and struck out former cls. (ii) to (iv) which read as follows:

''(ii) second to the portion of the passive activity credit to which subparagraph (B) or (D) does not apply,

''(iii) third to the portion of such credit to which subparagraph (B) applies,

''(iv) fourth to the portion of such loss to which subparagraph (C) applies, and''.

2001—Subsec. (i)(3)(F)(iii). Pub. L. 107–16 substituted '', 221, and 222'' for ''and 221''.

2000—Subsec. (i)(3)(C) to (F). Pub. L. 106–554, § 1(a)(7) [title I, § 101(b)(1), (2)], added subpar. (C), redesignated former subpars. (C) to (E) as (D) to (F), respectively, and generally amended heading and text of subpar. (E), as redesignated. Prior to amendment, text read as follows: ''If subparagraph (B) or (C) applies for any taxable year, paragraph (1) shall be applied—

''(i) first to the passive activity loss,

''(ii) second to the portion of the passive activity credit to which subparagraph (B) or (C) does not apply,

''(iii) third to the portion of such credit to which subparagraph (B) applies, and

''(iv) then to the portion of such credit to which subparagraph (C) applies.''

Subsec. (i)(6)(B). Pub. L. 106–554, §1(a)(7) [title I, §101(b)(3)(B)], substituted '', rehabilitation credit, or commercial revitalization deduction'' for ''or rehabilitation credit'' in heading.

Subsec. (i)(6)(B)(iii). Pub. L. 106–554, §1(a)(7) [title I, §101(b)(3)(A)], added cl. (iii).

1998—Subsec. (i)(3)(E)(iii). Pub. L. 105–277 amended cl. (iii) generally. Prior to amendment, cl. (iii) read as follows: ''any amount allowable as a deduction under section 219, and''.

1996—Subsec. (c)(3)(B). Pub. L. 104–188, §1704(d)(1), inserted at end ''If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27(a)) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income.''

Subsec. (g)(1)(A). Pub. L. 104–188, §1704(e)(1), reenacted heading without change and amended text generally. Prior to amendment, text read as follows: ''If all gain or loss realized on such disposition is recognized, the excess of—

''(i) the sum of—

''(I) any loss from such activity for such taxable year (determined after application of subsection (b)), plus

''(II) any loss realized on such disposition, over

''(ii) net income or gain for such taxable year from all passive activities (determined without regard to losses described in clause (i)),

shall be treated as a loss which is not from a passive activity.''

Subsec. (i)(3)(E)(ii). Pub. L. 104–188, §1807(c)(4), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: ''the amount excludable from gross income under section 135,''.

1993—Subsec. (c)(2). Pub. L. 103–66, §13143(b)(1), substituted ''Except as provided in paragraph (7), the'' for ''The''.

Subsec. (c)(7). Pub. L. 103–66, §13143(a), added par. (7).

Subsec. (i)(3)(E)(iv). Pub. L. 103–66, §13143(b)(2), inserted ''or any loss allowable by reason of subsection (c)(7)'' after ''loss''.

1990—Subsec. (i)(3)(B), (6)(B)(ii). Pub. L. 101–508, §11813(b)(16)(A), substituted ''rehabilitation credit determined under section 47'' for ''rehabilitation investment credit (within the meaning of section 48(*o*))''.

Subsec. (k)(1). Pub. L. 101–508, §11813(b)(16)(B), substituted ''rehabilitation credit determined under section 47'' for ''rehabilitation investment credit (within the meaning of section 48(*o*))''.

Subsec. (m)(3)(A). Pub. L. 101–508, §11704(a)(6), substituted ''pre-enactment'' for ''preenactment''.

1989—Subsec. (i)(3)(B), (C). Pub. L. 101–239 added subpars. (B) and (C) and struck out former subpars. (B) and (C) which read as follows:

''(B) SPECIAL PHASE-OUT OF LOW-INCOME HOUSING AND REHABILITATION CREDITS.—In the case of any portion of the passive activity credit for any taxable year which is attributable to any credit to which paragraph (6)(B) applies, subparagraph (A) shall be applied by substituting '$200,000' for '$100,000'.

''(C) ORDERING RULE TO REFLECT SEPARATE PHASE-OUTS.—If subparagraph (B) applies for any taxable year, paragraph (1) shall be applied—

''(i) first to the passive activity loss,

''(ii) second to the portion of the passive activity credit to which subparagraph (B) does not apply, and

''(iii) then to the portion of such credit to which subparagraph (B) applies.''

Subsec. (i)(3)(D), (E). Pub. L. 101–239 added subpar. (D) and redesignated former subpar. (D) as (E).

1988—Subsec. (e)(1)(A)(ii). Pub. L. 100–647, §1005(a)(1), inserted ''not derived in the ordinary course of a trade or business which is'' after ''gain or loss''.

Subsec. (g)(1)(A). Pub. L. 100–647, §1005(a)(2)(A), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''If all gain or loss realized on such disposition is recognized, any loss from such activity which has not previously been allowed as a deduction (and in the case of a passive activity for the taxable year, any loss realized on such disposition) shall not be treated as a passive activity loss and shall be allowable as a deduction against income in the following order:

''(i) Income or gain from the passive activity for the taxable year (including any gain recognized on the disposition).

''(ii) Net income or gain for the taxable year from all passive activities.

''(iii) Any other income or gain.''

Subsec. (g)(1)(C). Pub. L. 100–647, §1005(a)(2)(B), substituted ''Income from prior years'' for ''Coordination with section 1211'' in heading and amended text generally. Prior to amendment, text read as follows: ''In the case of any loss realized on the disposition of an interest in a passive activity, section 1211 shall be applied before subparagraph (A) is applied.''

Subsec. (g)(2)(A). Pub. L. 100–647, §1005(a)(3), substituted ''paragraph (1)(A)'' for ''paragraph (1)'' and ''to losses described in paragraph (1)(A)'' for ''to such losses''.

Subsec. (g)(3). Pub. L. 100–647, §1005(a)(4), substituted ''(realized or to be realized'' for ''realized (or to be realized)'' and ''is completed)'' for ''is completed''.

Subsec. (h)(4). Pub. L. 100–647, §1005(a)(5), inserted ''only'' before ''if''.

Subsec. (i)(1). Pub. L. 100–647, §1005(a)(6), substituted ''in such taxable year (and if any portion of such loss or credit arose in another taxable year, in such other taxable year)'' for ''in the taxable year in which such portion of such loss or credit arose''.

Subsec. (i)(3)(D). Pub. L. 100–647, §6009(c)(3), added cl. (ii) and redesignated former cls. (ii) and (iii) as (iii) and (iv), respectively.

Subsec. (i)(6)(C). Pub. L. 100–647, §1005(a)(7), substituted ''Except as provided in regulations, no'' for ''No''.

Subsec. (j)(6)(A). Pub. L. 100–647, §1005(a)(8), inserted ''with respect to which a deduction has not been allowed by reason of subsection (a)'' after ''to such interest''.

Subsec. (j)(10), (11). Pub. L. 100–647, §1005(a)(9), added pars. (10) and (11).

Subsec. (j)(12). Pub. L. 100–647, §1005(a)(11), added par. (12).

Subsec. (k)(3). Pub. L. 100–647, §2004(g), added par. (3).

Subsec. (m). Pub. L. 100–647, §1005(a)(12), substituted ''interest'' for ''interests'' in heading.

Subsec. (m)(1). Pub. L. 100–647, §1005(a)(12), added par. (1) and struck out former par. (1) which read as follows: ''In the case of any passive activity loss or credit for any taxable year beginning in calendar years 1987 through 1990 which—

''(A) is attributable to a pre-enactment interest, but

''(B) is not attributable to a carryforward to such taxable year of any loss or credit which was disallowed under this section for a preceding taxable year,

there shall be disallowed under subsection (a) only the applicable percentage of the amount which (but for this subsection) would have been disallowed under subsection (a) for such taxable year.''

Subsec. (m)(2). Pub. L. 100–647, §1005(a)(12), added par. (2) and struck out former par. (2) which resulted in substituting ''65'', ''40'', ''20'', and ''10'' for ''35'', ''60'', ''80'', and ''90'', respectively, in second column.

Subsec. (m)(3)(A). Pub. L. 100–647, §1005(a)(12), added subpar. (A) and struck out former subpar. (A) which read as follows: ''The portion of the passive activity loss for any taxable year which is attributable to pre-enactment interests shall be equal to the lesser of—

''(i) the passive activity loss for such taxable year, or

''(ii) the passive activity loss for such taxable year determined by taking into account only pre-enactment interests.

For purposes of this subparagraph, the deduction equivalent (within the meaning of subsection (j)(5)) of a passive activity credit shall be taken into account.''

1987—Subsecs. (k) to (m). Pub. L. 100–203 added subsec. (k) and redesignated former subsecs. (k) and (*l*) as (*l*) and (m), respectively.

EFFECTIVE DATE OF 2020 AMENDMENT

Amendment by Pub. L. 116–260 applicable to taxable years beginning after Dec. 31, 2020, see section 104(c) of div. EE of Pub. L. 116–260, set out as a note under section 25A of this title.

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by section 13305(b)(1) of Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, except as provided by transition rule, see section 13305(c) of Pub. L. 115–97, set out as a note under section 74 of this title.

Amendment by section 14202(b)(3) of Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, see section 14202(c) of Pub. L. 115–97, set out as a note under section 172 of this title.

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by section 221(a)(41)(G) of Pub. L. 113–295 not applicable to preferred stock issued before Oct. 1, 1942 (determined in the same manner as under section 247 of this title as in effect before its repeal by Pub. L. 113–295), see section 221(a)(41)(K) of Pub. L. 113–295, set out as a note under section 172 of this title.

Except as otherwise provided in section 221(a) of Pub. L. 113–295, amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by section 102(d)(5) of Pub. L. 108–357 applicable to taxable years beginning after Dec. 31, 2004, see section 102(e) of Pub. L. 108–357, set out as a note under section 56 of this title.

Pub. L. 108–357, title III, § 331(h), Oct. 22, 2004, 118 Stat. 1477, provided that: ''The amendments made by this section [amending this section and sections 851 and 7704 of this title] shall apply to taxable years beginning after the date of the enactment of this Act [Oct. 22, 2004].''

EFFECTIVE DATE OF 2002 AMENDMENT

Amendment by Pub. L. 107–147 effective as if included in the provisions of the Community Renewal Tax Relief Act of 2000 [H.R. 5662, as enacted by Pub. L. 106–554], to which such amendment relates, see section 412(e) of Pub. L. 107–147, set out as a note under section 151 of this title.

EFFECTIVE DATE OF 2001 AMENDMENT

Amendment by Pub. L. 107–16 applicable to payments made in taxable years beginning after Dec. 31, 2001, see section 431(d) of Pub. L. 107–16, set out as a note under section 62 of this title.

EFFECTIVE DATE OF 1998 AMENDMENT

Amendment by Pub. L. 105–277 effective as if included in the provision of the Taxpayer Relief Act of 1997, Pub. L. 105–34, to which such amendment relates, see section 4003(*l*) of Pub. L. 105–277, set out as a note under section 86 of this title.

EFFECTIVE DATE OF 1996 AMENDMENT

Pub. L. 104–188, title XVII, § 1704(d)(2), Aug. 20, 1996, 110 Stat. 1878, provided that: ''The amendment made by paragraph (1) [amending this section] shall apply to taxable years beginning after December 31, 1986.''

Pub. L. 104–188, title XVII, § 1704(e)(2), Aug. 20, 1996, 110 Stat. 1879, provided that: ''The amendment made by paragraph (1) [amending this section] shall apply to taxable years beginning after December 31, 1986.''

Amendment by section 1807(c)(4) of Pub. L. 104–188 applicable to taxable years beginning after Dec. 31, 1996, see section 1807(e) of Pub. L. 104–188, set out as an Effective Date note under section 23 of this title.

EFFECTIVE DATE OF 1993 AMENDMENT

Pub. L. 103–66, title XIII, § 13143(c), Aug. 10, 1993, 107 Stat. 441, provided that: ''The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1993.''

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by section 11813(b)(16) of Pub. L. 101–508 applicable to property placed in service after Dec. 31, 1990, but not applicable to any transition property (as defined in section 49(e) of this title), any property with respect to which qualified progress expenditures were previously taken into account under section 46(d) of this title, and any property described in section 46(b)(2)(C) of this title, as such sections were in effect on Nov. 4, 1990, see section 11813(c) of Pub. L. 101–508, set out as a note under section 45K of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Pub. L. 101–239, title VII, § 7109(b), Dec. 19, 1989, 103 Stat. 2322, provided that:

''(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [amending this section] shall apply to property placed in service after December 31, 1989, in taxable years ending after such date.

''(2) SPECIAL RULE WHERE INTEREST HELD IN PASS-THRU ENTITY.—In the case of a taxpayer who holds an indirect interest in property described in paragraph (1), the amendments made by this section shall apply only if such interest is acquired after December 31, 1989.''

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1005(a)(1)–(9), (11), (12) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Amendment by section 2004(g) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provisions of the Revenue Act of 1987, Pub. L. 100–203, title X, to which such amendment relates, see section 2004(u) of Pub. L. 100–647, set out as a note under section 56 of this title.

Amendment by section 6009(c)(3) of Pub. L. 100–647 applicable to taxable years beginning after Dec. 31, 1989, see section 6009(d) of Pub. L. 100–647, set out as a note under section 86 of this title.

EFFECTIVE DATE OF 1987 AMENDMENT

Amendment by Pub. L. 100–203 effective as if included in the amendments made by section 501 of the Tax Reform Act of 1986, Pub. L. 99–514, see section 10212(c) of Pub. L. 100–203, set out as a note under section 58 of this title.

EFFECTIVE DATE

Pub. L. 99–514, title V, § 501(c), Oct. 22, 1986, 100 Stat. 2241, as amended by Pub. L. 100–647, title I, § 1005(a)(10), title IV, § 4003(b)(2), Nov. 10, 1988, 102 Stat. 3388, 3644, provided that:

''(1) IN GENERAL.—The amendments made by this section [enacting this section] shall apply to taxable years beginning after December 31, 1986.

''(2) SPECIAL RULE FOR CARRYOVERS.—The amendments made by this section shall not apply to any loss, deduction, or credit carried to a taxable year beginning after December 31, 1986, from a taxable year beginning before January 1, 1987.

''[(3) Repealed. Pub. L. 100–647, title IV, § 4003(b)(2), Nov. 10, 1988, 102 Stat. 3644.]

''(4) INCOME FROM SALES OF PASSIVE ACTIVITIES IN TAXABLE YEARS BEGINNING BEFORE JANUARY 1, 1987.—If—

''(A) gain is recognized in a taxable year beginning after December 31, 1986, from a sale or exchange of an interest in an activity in a taxable year beginning before January 1, 1987, and

''(B) such gain would have been treated as gain from a passive activity had section 469 of the Internal Revenue Code of 1986 (as added by this section) been in effect for the taxable year in which the sale or exchange occurred and for all succeeding taxable years,

then such gain shall be treated as gain from a passive activity for purposes of such section.''

SAVINGS PROVISION

Amendment by section 401(d)(5)(B)(i)–(iii) of Pub. L. 115–141 not applicable to certain qualified community assets acquired, wages paid or incurred, qualified revitalization buildings placed in service, or property acquired before Jan. 1, 2010, see section 401(d)(5)(C) of Pub. L. 115–141, set out as a note under former section 1400E of this title.

For provisions that nothing in amendment by Pub. L. 115–141 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Mar. 23, 2018, for purposes of determining liability for tax for periods ending after Mar. 23, 2018, see section 401(e) of Pub. L. 115–141, set out as a note under section 23 of this title.

For provisions that nothing in amendment by section 11813(b)(16) of Pub. L. 101–508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101–508, set out as a note under section 45K of this title.

AMOUNTS ATTRIBUTABLE TO ACTIVITIES SUBJECT TO LIMITATIONS UNDER SECTION 469 TREATED AS DEDUCTION ALLOCABLE TO SUCH ACTIVITY

Pub. L. 100–647, title I, §1005(c)(11), Nov. 10, 1988, 102 Stat. 3392, provided that: ''If—

''(A) any amount was disallowed as a deduction under section 163(d) of the Internal Revenue Code of 1954 [now 1986] (as in effect on the day before the date of the enactment of the Reform Act [Oct. 22, 1986]),

''(B) such amount would (but for this paragraph) be treated as investment interest paid or accrued by the taxpayer in the taxpayer's first taxable year beginning after December 31, 1986, and

''(C) the taxpayer makes an election under this paragraph at such time and in such manner as the Secretary of the Treasury or his delegate shall prescribe,

to the extent such amount is attributable to an activity subject to the limitations of section 469 of the 1986 Code, such amount shall not be treated as investment interest but shall be treated as a deduction allocable to such activity for such first taxable year. [Former] Subsection (m) of section 469 of the 1986 Code and section 501(c)(2) of the Reform Act [Pub. L. 99–514, set out as an Effective Date note above] shall not apply to any amount so treated.''

TRANSITIONAL RULE FOR LOW-INCOME HOUSING

Pub. L. 99–514, title V, §502, Oct. 22, 1986, 100 Stat. 2241, as amended by Pub. L. 99–509, title VIII, §8073(a), Oct. 21, 1986, 100 Stat. 1965; Pub. L. 100–647, title I, §1005(b), Nov. 10, 1988, 102 Stat. 3389, provided that:

''(a) GENERAL RULE.—Any loss sustained by a qualified investor with respect to an interest in a qualified low-income housing project for any taxable year in the relief period shall not be treated as a loss from a passive activity for purposes of section 469 of the Internal Revenue Code of 1986.

''(b) RELIEF PERIOD.—For purposes of subsection (a), the term 'relief period' means the period beginning with the taxable year in which the investor made his initial investment in the qualified low-income housing project and ending with whichever of the following is the earliest—

''(1) the 6th taxable year after the taxable year in which the investor made his initial investment,

''(2) the 1st taxable year after the taxable year in which the investor is obligated to make his last investment, or

''(3) the taxable year preceding the 1st taxable year for which such project ceased to be a qualified low-income housing project.

''(c) QUALIFIED LOW-INCOME HOUSING PROJECT.—For purposes of this section, the term 'qualified low-income housing project' means any project if—

''(1) such project meets the requirements of clause (i), (ii), (iii), or (iv) of section 1250(a)(1)(B) [of the Internal Revenue Code of 1986] as of the date placed in service and for each taxable year thereafter which begins after 1986 and for which a passive loss may be allowable with respect to such project,

''(2) the operator certifies to the Secretary of the Treasury or his delegate that such project met the requirements of paragraph (1) on the date of the enactment of this Act [Oct. 22, 1986] (or, if later, when placed in service) and annually thereafter,

''(3) such project is constructed or acquired pursuant to a binding written contract entered into on or before August 16, 1986, and

''(4) such project is placed in service before January 1, 1989.

''(d) QUALIFIED INVESTOR.—For purposes of this section—

''(1) IN GENERAL.—The term 'qualified investor' means any natural person who holds (directly or through 1 or more entities) an interest in a qualified low-income housing project—

''(A) if—

''(i) in the case of a project placed in service on or before August 16, 1986, such person held an interest in such project on August 16, 1986, and such person made his initial investment after December 31, 1983, or

''(ii) in the case of a project placed in service after August 16, 1986, such person made his initial investment after December 31, 1983, and such person held an interest in such project on December 31, 1986, and

''(B) if such investor is required to make payments after December 31, 1986, of 50 percent or more of the total original obligated investment for such interest.

For purposes of subparagraph (A), a person shall be treated as holding an interest on August 16, 1986, or December 31, 1986, if on such date such person had a binding contract to acquire such interest.

''(2) TREATMENT OF ESTATES.—The estate of a decedent shall succeed to the treatment under this section of the decedent but only with respect to the 1st 2 taxable years of such estate ending after the date of the decedent's death.

''(3) SPECIAL RULE FOR CERTAIN PARTNERSHIPS.—In the case of any property which is held by a partnership—

''(A) which placed such property in service on or after December 31, 1985, and before August 17, 1986, and continuously held such property through the close of the taxable year for which the determination is being made, and

''(B) which was not treated as a new partnership or as terminated at any time on or after the date on which such property was placed in service and through the close of the taxable year for which the determination is being made,

paragraph (1)(A)(i) shall be applied by substituting 'December 31, 1988' for 'August 16, 1986' the 2nd place it appears.

''(4) SPECIAL RULE FOR CERTAIN RURAL HOUSING.—In the case of any interest in a qualified low-income housing project which—

''(A) is assisted under section 515 of the Housing Act of 1949 [42 U.S.C. 1485] (relating to the Farmers' Home Administration Program), and

''(B) is located in a town with a population of less than 10,000 and which is not part of a metropolitan statistical area,

paragraph (1)(B) shall be applied by substituting '35 percent' for '50 percent' and subsection (b)(1) shall be applied by substituting '5th taxable year' for '6th taxable year'. The preceding sentence shall not apply to any interest unless, on December 31, 1986, at least one-half of the number of payments required with respect to such interest remain to be paid.

''(e) SPECIAL RULES.—

''(1) WHERE MORE THAN 1 BUILDING IN PROJECT.—If there is more than 1 building in any project, the determination of when such project is placed in service shall be based on when the 1st building in such project is placed in service.

''(2) ONLY CASH AND OTHER PROPERTY TAKEN INTO ACCOUNT.—In determining the amount any person invests in (or is obligated to invest in) any interest, only cash and other property shall be taken into account.

''(3) COORDINATION WITH CREDIT.—No low-income housing credit shall be determined under section 42 of the Internal Revenue Code of 1986 with respect to any project with respect to which any person has been allowed any benefit under this section.''

[Pub. L. 99–509, title VIII, § 8073(b), Oct. 21, 1986, 100 Stat. 1965, provided that: ''The amendment made by subsection (a) [amending section 502 of Pub. L. 99–514, set out above] shall take effect as if included in section 502 of the Tax Reform Act of 1986 on the date of its enactment [Oct. 22, 1986].'']

§ 470. Limitation on deductions allocable to property used by governments or other tax-exempt entities

(a) Limitation on losses

Except as otherwise provided in this section, a tax-exempt use loss for any taxable year shall not be allowed.

(b) Disallowed loss carried to next year

Any tax-exempt use loss with respect to any tax-exempt use property which is disallowed under subsection (a) for any taxable year shall be treated as a deduction with respect to such property in the next taxable year.

(c) Definitions

For purposes of this section—

(1) Tax-exempt use loss

The term ''tax-exempt use loss'' means, with respect to any taxable year, the amount (if any) by which—

(A) the sum of—

(i) the aggregate deductions (other than interest) directly allocable to a tax-exempt use property, plus

(ii) the aggregate deductions for interest properly allocable to such property, exceed

(B) the aggregate income from such property.

(2) Tax-exempt use property

(A) In general

The term ''tax-exempt use property'' has the meaning given to such term by section 168(h), except that such section shall be applied—

(i) without regard to paragraphs (1)(C) and (3) thereof, and

(ii) as if section 197 intangible property (as defined in section 197), and property described in paragraph (1)(B) or (2) of section 167(f), were tangible property.

(B) Exception for partnerships

Such term shall not include any property which would (but for this subparagraph) be tax-exempt use property solely by reason of section 168(h)(6).

(C) Cross reference

For treatment of partnerships as leases to which section 168(h) applies, see section 7701(e).

(d) Exception for certain leases

This section shall not apply to any lease of property which meets the requirements of all of the following paragraphs:

(1) Availability of funds

(A) In general

A lease of property meets the requirements of this paragraph if (at all times during the lease term) not more than an allowable amount of funds are—

(i) subject to any arrangement referred to in subparagraph (B), or

(ii) set aside or expected to be set aside,

to or for the benefit of the lessor or any lender, or to or for the benefit of the lessee to satisfy the lessee's obligations or options under the lease. For purposes of clause (ii), funds shall be treated as set aside or expected to be set aside only if a reasonable person would conclude, based on the facts and circumstances, that such funds are set aside or expected to be set aside.

(B) Arrangements

The arrangements referred to in this subparagraph include a defeasance arrangement, a loan by the lessee to the lessor or any lender, a deposit arrangement, a letter of credit collateralized with cash or cash equivalents, a payment undertaking agreement, prepaid rent (within the meaning of the regulations under section 467), a sinking fund arrangement, a guaranteed investment contract, financial guaranty insurance, and any similar arrangement (whether or not such arrangement provides credit support).

(C) Allowable amount

(i) In general

Except as otherwise provided in this subparagraph, the term ''allowable amount'' means an amount equal to 20 percent of the lessor's adjusted basis in the property at the time the lease is entered into.

(ii) Higher amount permitted in certain cases

To the extent provided in regulations, a higher percentage shall be permitted under clause (i) where necessary because of the credit-worthiness of the lessee. In no event may such regulations permit a percentage of more than 50 percent.

(iii) Option to purchase

If under the lease the lessee has the option to purchase the property for a fixed price or for other than the fair market value of the property (determined at the

time of exercise), the allowable amount at the time such option may be exercised may not exceed 50 percent of the price at which such option may be exercised.

(iv) No allowable amount for certain arrangements

The allowable amount shall be zero with respect to any arrangement which involves—

(I) a loan from the lessee to the lessor or a lender,

(II) any deposit received, letter of credit issued, or payment undertaking agreement entered into by a lender otherwise involved in the transaction, or

(III) in the case of a transaction which involves a lender, any credit support made available to the lessor in which any such lender does not have a claim that is senior to the lessor.

For purposes of subclause (I), the term ''loan'' shall not include any amount treated as a loan under section 467 with respect to a section 467 rental agreement.

(2) Lessor must make substantial equity investment

(A) In general

A lease of property meets the requirements of this paragraph if—

(i) the lessor—

(I) has at the time the lease is entered into an unconditional at-risk equity investment (as determined by the Secretary) in the property of at least 20 percent of the lessor's adjusted basis in the property as of that time, and

(II) maintains such investment throughout the term of the lease, and

(ii) the fair market value of the property at the end of the lease term is reasonably expected to be equal to at least 20 percent of such basis.

(B) Risk of loss

For purposes of subparagraph (A)(ii), the fair market value at the end of the lease term shall be reduced to the extent that a person other than the lessor bears a risk of loss in the value of the property.

(C) Paragraph not to apply to short-term leases

This paragraph shall not apply to any lease with a lease term of 5 years or less.

(3) Lessee may not bear more than minimal risk of loss

(A) In general

A lease of property meets the requirements of this paragraph if there is no arrangement under which the lessee bears—

(i) any portion of the loss that would occur if the fair market value of the leased property were 25 percent less than its reasonably expected fair market value at the time the lease is terminated, or

(ii) more than 50 percent of the loss that would occur if the fair market value of the leased property at the time the lease is terminated were zero.

(B) Exception

The Secretary may by regulations provide that the requirements of this paragraph are not met where the lessee bears more than a minimal risk of loss.

(C) Paragraph not to apply to short-term leases

This paragraph shall not apply to any lease with a lease term of 5 years or less.

(4) Property with more than 7-year class life

In the case of a lease—

(A) of property with a class life (as defined in section 168(i)(1)) of more than 7 years, other than fixed-wing aircraft and vessels, and

(B) under which the lessee has the option to purchase the property,

the lease meets the requirements of this paragraph only if the purchase price under the option equals the fair market value of the property (determined at the time of exercise).

(e) Special rules

(1) Treatment of former tax-exempt use property

(A) In general

In the case of any former tax-exempt use property—

(i) any deduction allowable under subsection (b) with respect to such property for any taxable year shall be allowed only to the extent of any net income (without regard to such deduction) from such property for such taxable year, and

(ii) any portion of such unused deduction remaining after application of clause (i) shall be treated as a deduction allowable under subsection (b) with respect to such property in the next taxable year.

(B) Former tax-exempt use property

For purposes of this subsection, the term ''former tax-exempt use property'' means any property which—

(i) is not tax-exempt use property for the taxable year, but

(ii) was tax-exempt use property for any prior taxable year.

(2) Disposition of entire interest in property

If during the taxable year a taxpayer disposes of the taxpayer's entire interest in tax-exempt use property (or former tax-exempt use property), rules similar to the rules of section 469(g) shall apply for purposes of this section.

(3) Coordination with section 469

This section shall be applied before the application of section 469.

(4) Coordination with sections 1031 and 1033

(A) In general

Sections 1031(a) and 1033(a) shall not apply if—

(i) the exchanged or converted property is tax-exempt use property subject to a lease which was entered into before March 13, 2004, and which would not have met the requirements of subsection (d) had such re-

quirements been in effect when the lease was entered into, or

(ii) the replacement property is tax-exempt use property subject to a lease which does not meet the requirements of subsection (d).

(B) Adjusted basis

In the case of property acquired by the lessor in a transaction to which section 1031 or 1033 applies, the adjusted basis of such property for purposes of this section shall be equal to the lesser of—

(i) the fair market value of the property as of the beginning of the lease term, or

(ii) the amount which would be the lessor's adjusted basis if such sections did not apply to such transaction.

(f) Other definitions

For purposes of this section—

(1) Related parties

The terms ''lessor'', ''lessee'', and ''lender'' each include any related party (within the meaning of section 197(f)(9)(C)(i)).

(2) Lease term

The term ''lease term'' has the meaning given to such term by section 168(i)(3).

(3) Lender

The term ''lender'' means, with respect to any lease, a person that makes a loan to the lessor which is secured (or economically similar to being secured) by the lease or the leased property.

(4) Loan

The term ''loan'' includes any similar arrangement.

(g) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations which—

(1) allow in appropriate cases the aggregation of property subject to the same lease, and

(2) provide for the determination of the allocation of interest expense for purposes of this section.

(Added Pub. L. 108–357, title VIII, § 848(a), Oct. 22, 2004, 118 Stat. 1602; amended Pub. L. 110–172, § 7(c), Dec. 29, 2007, 121 Stat. 2482; Pub. L. 115–141, div. U, title IV, § 401(a)(120), Mar. 23, 2018, 132 Stat. 1190.)

AMENDMENTS

2018—Subsec. (d)(2)(B). Pub. L. 115–141 substituted ''subparagraph (A)(ii)'' for ''clause (ii)''.

2007—Subsec. (c)(2). Pub. L. 110–172, § 7(c)(1), reenacted heading without change and amended text generally. Prior to amendment, text read as follows: ''The term 'tax-exempt use property' has the meaning given to such term by section 168(h), except that such section shall be applied—

''(A) without regard to paragraphs (1)(C) and (3) thereof, and

''(B) as if property described in—

''(i) section 167(f)(1)(B),

''(ii) section 167(f)(2), and

''(iii) section 197 intangible,

were tangible property.

Such term shall not include property which would (but for this sentence) be tax-exempt use property solely by reason of section 168(h)(6) if any credit is allowable under section 42 or 47 with respect to such property.''

Subsec. (d)(1)(A). Pub. L. 110–172, § 7(c)(2), in introductory provisions, substituted ''(at all times during the lease term)'' for ''(at any time during the lease term)''.

EFFECTIVE DATE OF 2007 AMENDMENT

Amendment by Pub. L. 110–172 effective as if included in the provision of the American Jobs Creation Act of 2004, Pub. L. 108–357, to which such amendment relates, see section 7(e) of Pub. L. 110–172, set out as a note under section 1092 of this title.

EFFECTIVE DATE

Pub. L. 108–357, title VIII, § 849, Oct. 22, 2004, 118 Stat. 1606, as amended by Pub. L. 109–135, title IV, § 403(ff), Dec. 21, 2005, 119 Stat. 2631, provided that:

''(a) IN GENERAL.—Except as provided in this section, the amendments made by this part [part III (§§ 847–849) of subtitle B of title VIII of Pub. L. 108–357, enacting this section and amending sections 167, 168, and 197 of this title] shall apply to leases entered into after March 12, 2004, and in the case of property treated as tax-exempt use property other than by reason of a lease, to property acquired after March 12, 2004.

''(b) EXCEPTION.—

''(1) IN GENERAL.—The amendments made by this part shall not apply to qualified transportation property.

''(2) QUALIFIED TRANSPORTATION PROPERTY.—For purposes of paragraph (1), the term 'qualified transportation property' means domestic property subject to a lease with respect to which a formal application—

''(A) was submitted for approval to the Federal Transit Administration (an agency of the Department of Transportation) after June 30, 2003, and before March 13, 2004,

''(B) is approved by the Federal Transit Administration before January 1, 2006, and

''(C) includes a description of such property and the value of such property.

''(3) EXCHANGES AND CONVERSION OF TAX-EXEMPT USE PROPERTY.—Section 470(e)(4) of the Internal Revenue Code of 1986, as added by section 848, shall apply to property exchanged or converted after the date of the enactment of this Act [Oct. 22, 2004].

''(4) INTANGIBLES AND INDIAN TRIBAL GOVERNMENTS.—The amendments made subsections (b)(2), (b)(3), and (e) of section 847 [amending sections 167, 168, and 197 of this title], and the treatment of property described in clauses (ii) and (iii) of section 470(c)(2)(B) of the Internal Revenue Code of 1986 (as added by section 848) as tangible property, shall apply to leases entered into after October 3, 2004.''

SUBPART D—INVENTORIES

Sec.

AMENDMENTS

1993—Pub. L. 103–66, title XIII, § 13223(b)(2), Aug. 10, 1993, 107 Stat. 484, added item 475.

1986—Pub. L. 99–514, title VIII, § 802(b), Oct. 22, 1986, 100 Stat. 2350, substituted ''Simplified dollar-value LIFO method for certain small businesses'' for ''Election by certain small businesses to use one inventory pool'' in item 474.

1981—Pub. L. 97–34, title II, § 237(b), Aug. 13, 1981, 95 Stat. 253, added item 474.

1980—Pub. L. 96–223, title IV, § 403(a)(2), Apr. 2, 1980, 94 Stat. 304, added item 473.

§ 471. General rule for inventories

(a) General rule

Whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the Secretary may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.

(b) Estimates of inventory shrinkage permitted

A method of determining inventories shall not be treated as failing to clearly reflect income solely because it utilizes estimates of inventory shrinkage that are confirmed by a physical count only after the last day of the taxable year if—

(1) the taxpayer normally does a physical count of inventories at each location on a regular and consistent basis, and

(2) the taxpayer makes proper adjustments to such inventories and to its estimating methods to the extent such estimates are greater than or less than the actual shrinkage.

(c) Exemption for certain small businesses

(1) In general

In the case of any taxpayer (other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under section 448(a)(3)) which meets the gross receipts test of section 448(c) for any taxable year—

(A) subsection (a) shall not apply with respect to such taxpayer for such taxable year, and

(B) the taxpayer's method of accounting for inventory for such taxable year shall not be treated as failing to clearly reflect income if such method either—

(i) treats inventory as non-incidental materials and supplies, or

(ii) conforms to such taxpayer's method of accounting reflected in an applicable financial statement of the taxpayer with respect to such taxable year or, if the taxpayer does not have any applicable financial statement with respect to such taxable year, the books and records of the taxpayer prepared in accordance with the taxpayer's accounting procedures.

(2) Applicable financial statement

For purposes of this subsection, the term ''applicable financial statement'' has the meaning given the term in section 451(b)(3).

(3) Application of gross receipts test to individuals, etc.

In the case of any taxpayer which is not a corporation or a partnership, the gross receipts test of section 448(c) shall be applied in the same manner as if each trade or business of such taxpayer were a corporation or partnership.

(4) Coordination with section 481

Any change in method of accounting made pursuant to this subsection shall be treated for purposes of section 481 as initiated by the taxpayer and made with the consent of the Secretary.

(d) Cross reference

For rules relating to capitalization of direct and indirect costs of property, see section 263A.

(Aug. 16, 1954, ch. 736, 68A Stat. 159; Pub. L. 94–455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 99–514, title VIII, §803(b)(4), Oct. 22, 1986, 100 Stat. 2356; Pub. L. 105–34, title IX, §961(a), Aug. 5, 1997, 111 Stat. 891; Pub. L. 115–97, title I, §13102(c), Dec. 22, 2017, 131 Stat. 2103.)

AMENDMENTS

2017—Subsecs. (c), (d). Pub. L. 115–97 added subsec. (c) and redesignated former subsec. (c) as (d).

1997—Subsecs. (b), (c). Pub. L. 105–34 added subsec. (b) and redesignated former subsec. (b) as (c).

1986—Pub. L. 99–514 designated existing provisions as subsec. (a) and added subsec. (b).

1976—Pub. L. 94–455 struck out ''or his delegate'' after ''Secretary'' wherever appearing.

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to taxable years beginning after Dec. 31, 2017, see section 13102(e) of Pub. L. 115–97, set out as a note under section 263A of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105–34, title IX, §961(b)(1), Aug. 5, 1997, 111 Stat. 891, provided that: ''The amendment made by this section [amending this section] shall apply to taxable years ending after the date of the enactment of this Act [Aug. 5, 1997].''

EFFECTIVE DATE OF 1986 AMENDMENT

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the amendment by Pub. L. 99–514 is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99–514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101–239, set out as an Effective Date note under section 263A of this title.

Amendment by Pub. L. 99–514 applicable to costs incurred after Dec. 31, 1986, in taxable years ending after such date, except as otherwise provided, see section 803(d) of Pub. L. 99–514, set out as an Effective Date note under section 263A of this title.

COORDINATION WITH SECTION 481

Pub. L. 105–34, title IX, §961(b)(2), Aug. 5, 1997, 111 Stat. 891, provided that: ''In the case of any taxpayer permitted by this section [amending this section and enacting provisions set out as a note above] to change its method of accounting to a permissible method for any taxable year—

''(A) such changes shall be treated as initiated by the taxpayer,

''(B) such changes shall be treated as made with the consent of the Secretary of the Treasury, and

''(C) the period for taking into account the adjustments under section 481 [26 U.S.C. 481] by reason of such change shall be 4 years.''

STUDY OF ACCOUNTING METHODS FOR INVENTORY; REPORT NOT LATER THAN DECEMBER 31, 1982

Pub. L. 97–34, title II, §238, Aug. 13, 1981, 95 Stat. 254, directed Secretary of the Treasury to conduct a study of methods of tax accounting for inventory with a view towards development of simplified methods and to re-

port to Congress, not later than Dec. 31, 1982, prior to repeal by Pub. L. 100–647, title VI, § 6252(a)(2), Nov. 10, 1988, 102 Stat. 3752.

§ 472. Last-in, first-out inventories

(a) Authorization

A taxpayer may use the method provided in subsection (b) (whether or not such method has been prescribed under section 471) in inventorying goods specified in an application to use such method filed at such time and in such manner as the Secretary may prescribe. The change to, and the use of, such method shall be in accordance with such regulations as the Secretary may prescribe as necessary in order that the use of such method may clearly reflect income.

(b) Method applicable

In inventorying goods specified in the application described in subsection (a), the taxpayer shall:

(1) Treat those remaining on hand at the close of the taxable year as being: First, those included in the opening inventory of the taxable year (in the order of acquisition) to the extent thereof; and second, those acquired in the taxable year;

(2) Inventory them at cost; and

(3) Treat those included in the opening inventory of the taxable year in which such method is first used as having been acquired at the same time and determine their cost by the average cost method.

(c) Condition

Subsection (a) shall apply only if the taxpayer establishes to the satisfaction of the Secretary that the taxpayer has used no procedure other than that specified in paragraphs (1) and (3) of subsection (b) in inventorying such goods to ascertain the income, profit, or loss of the first taxable year for which the method described in subsection (b) is to be used, for the purpose of a report or statement covering such taxable year—

(1) to shareholders, partners, or other proprietors, or to beneficiaries, or

(2) for credit purposes.

(d) 3-year averaging for increases in inventory value

The beginning inventory for the first taxable year for which the method described in subsection (b) is used shall be valued at cost. Any change in the inventory amount resulting from the application of the preceding sentence shall be taken into account ratably in each of the 3 taxable years beginning with the first taxable year for which the method described in subsection (b) is first used.

(e) Subsequent inventories

If a taxpayer, having complied with subsection (a), uses the method described in subsection (b) for any taxable year, then such method shall be used in all subsequent taxable years unless—

(1) with the approval of the Secretary a change to a different method is authorized; or,

(2) the Secretary determines that the taxpayer has used for any such subsequent taxable year some procedure other than that specified in paragraph (1) of subsection (b) in inventorying the goods specified in the application to ascertain the income, profit, or loss of such subsequent taxable year for the purpose of a report or statement covering such taxable year (A) to shareholders, partners, or other proprietors, or beneficiaries, or (B) for credit purposes; and requires a change to a method different from that prescribed in subsection (b) beginning with such subsequent taxable year or any taxable year thereafter.

If paragraph (1) or (2) of this subsection applies, the change to, and the use of, the different method shall be in accordance with such regulations as the Secretary may prescribe as necessary in order that the use of such method may clearly reflect income.

(f) Use of government price indexes in pricing inventory

The Secretary shall prescribe regulations permitting the use of suitable published governmental indexes in such manner and circumstances as determined by the Secretary for purposes of the method described in subsection (b).

(g) Conformity rules applied on controlled group basis

(1) In general

Except as otherwise provided in regulations, all members of the same group of financially related corporations shall be treated as 1 taxpayer for purposes of subsections (c) and (e)(2).

(2) Group of financially related corporations

For purposes of paragraph (1), the term ''group of financially related corporations'' means—

(A) any affiliated group as defined in section 1504 determined by substituting ''50 percent'' for ''80 percent'' each place it appears in section 1504(a) and without regard to section 1504(b), and

(B) any other group of corporations which consolidate or combine for purposes of financial statements.

(Aug. 16, 1954, ch. 736, 68A Stat. 159; Pub. L. 94–455, title XIX, §§ 1901(b)(36)(A), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1802, 1834; Pub. L. 97–34, title II, §§ 235, 236(a), Aug. 13, 1981, 95 Stat. 252; Pub. L. 98–369, div. A, title I, § 95(a), July 18, 1984, 98 Stat. 616.)

AMENDMENTS

1984—Subsec. (g). Pub. L. 98–369 added subsec. (g).

1981—Subsec. (d). Pub. L. 97–34, § 236(a), substituted ''3-year averaging for increases in inventory value'' for ''Preceding closing inventory'' in heading, substituted first sentence reading ''The beginning inventory for the first taxable year for which the method described in subsection (b) is used shall be valued at cost.'' for ''In determining income for the taxable year preceding the taxable year for which the method described in subsection (b) is first used, the closing inventory of such preceding year of the goods specified in the application referred to in subsection (a) shall be at cost.'' and inserted ''Any change in the inventory amount resulting from the application of the preceding sentence shall be taken into account ratably in each of the 3 taxable years beginning with the first taxable year for which the method described in subsection (b) is first used.''

Subsec. (f). Pub. L. 97–34, § 235, added subsec. (f).

1976—Subsecs. (a), (c), (e). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary'' wherever appearing.

Subsec. (f). Pub. L. 94–455, §1901(b)(36)(A), struck out subsec. (f) which provided for a cross reference relating to involuntary liquidation and replacement of LIFO inventories.

EFFECTIVE DATE OF 1984 AMENDMENT

Pub. L. 98–369, div. A, title I, §95(b), July 18, 1984, 98 Stat. 616, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after the date of the enactment of this Act [July 18, 1984].''

EFFECTIVE DATE OF 1981 AMENDMENT

Pub. L. 97–34, title II, §236(b), Aug. 13, 1981, 95 Stat. 252, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1981.''

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(b)(36)(A) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

§ 473. Qualified liquidations of LIFO inventories

(a) General rule

If, for any liquidation year—

(1) there is a qualified liquidation of goods which the taxpayer inventories under the LIFO method, and

(2) the taxpayer elects to have the provisions of this section apply with respect to such liquidation,

then the gross income of the taxpayer for such taxable year shall be adjusted as provided in subsection (b).

(b) Adjustment for replacements

If the liquidated goods are replaced (in whole or in part) during any replacement year and such replacement is reflected in the closing inventory for such year, then the gross income for the liquidation year shall be—

(1) decreased by an amount equal to the excess of—

(A) the aggregate replacement cost of the liquidated goods so replaced during such year, over

(B) the aggregate cost of such goods reflected in the opening inventory of the liquidation year, or

(2) increased by an amount equal to the excess of—

(A) the aggregate cost reflected in such opening inventory of the liquidated goods so replaced during such year, over

(B) such aggregate replacement cost.

(c) Qualified liquidation defined

For purposes of this section—

(1) In general

The term ''qualified liquidation'' means—

(A) a decrease in the closing inventory of the liquidation year from the opening inventory of such year, but only if

(B) the taxpayer establishes to the satisfaction of the Secretary that such decrease is directly and primarily attributable to a qualified inventory interruption.

(2) Qualified inventory interruption defined

(A) In general

The term ''qualified inventory interruption'' means a regulation, request, or interruption described in subparagraph (B) but only to the extent provided in the notice published pursuant to subparagraph (B).

(B) Determination by Secretary

Whenever the Secretary, after consultation with the appropriate Federal officers, determines—

(i) that—

(I) any Department of Energy regulation or request with respect to energy supplies, or

(II) any embargo, international boycott, or other major foreign trade interruption,

has made difficult or impossible the replacement during the liquidation year of any class of goods for any class of taxpayers, and

(ii) that the application of this section to that class of goods and taxpayers is necessary to carry out the purposes of this section,

he shall publish a notice of such determinations in the Federal Register, together with the period to be affected by such notice.

(d) Other definitions and special rules

For purposes of this section—

(1) Liquidation year

The term ''liquidation year'' means the taxable year in which occurs the qualified liquidation to which this section applies.

(2) Replacement year

The term ''replacement year'' means any taxable year in the replacement period; except that such term shall not include any taxable year after the taxable year in which replacement of the liquidated goods is completed.

(3) Replacement period

The term ''replacement period'' means the shorter of—

(A) the period of the 3 taxable years following the liquidation year, or

(B) the period specified by the Secretary in a notice published in the Federal Register with respect to that qualified inventory interruption.

Any period specified by the Secretary under subparagraph (B) may be modified by the Secretary in a subsequent notice published in the Federal Register.

(4) LIFO method

The term ''LIFO method'' means the method of inventorying goods described in section 472.

(5) Election

(A) In general

An election under subsection (a) shall be made subject to such conditions, and in such manner and form and at such time, as the Secretary may prescribe by regulation.

(B) Irrevocable election

An election under this section shall be irrevocable and shall be binding for the liq-

uidation year and for all determinations for prior and subsequent taxable years insofar as such determinations are affected by the adjustments under this section.

(e) Replacement; inventory basis

For purposes of this chapter—

(1) Replacements

If the closing inventory of the taxpayer for any replacement year reflects an increase over the opening inventory of such goods for such year, the goods reflecting such increase shall be considered, in the order of their acquisition, as having been acquired in replacement of the goods most recently liquidated (whether or not in a qualified liquidation) and not previously replaced.

(2) Amount at which replacement goods taken into account

In the case of any qualified liquidation, any goods considered under paragraph (1) as having been acquired in replacement of the goods liquidated in such liquidation shall be taken into purchases and included in the closing inventory of the taxpayer for the replacement year at the inventory cost basis of the goods replaced.

(f) Special rules for application of adjustments

(1) Period of limitations

If—

(A) an adjustment is required under this section for any taxable year by reason of the replacement of liquidated goods during any replacement year, and

(B) the assessment of a deficiency, or the allowance of a credit or refund of an overpayment of tax attributable to such adjustment, for any taxable year, is otherwise prevented by the operation of any law or rule of law (other than section 7122, relating to compromises),

then such deficiency may be assessed, or credit or refund allowed, within the period prescribed for assessing a deficiency or allowing a credit or refund for the replacement year if a notice for deficiency is mailed, or claim for refund is filed, within such period.

(2) Interest

Solely for purposes of determining interest on any overpayment or underpayment attributable to an adjustment made under this section, such overpayment or underpayment shall be treated as an overpayment or underpayment (as the case may be) for the replacement year.

(g) Coordination with section 472

The Secretary shall prescribe such regulations as may be necessary to coordinate the provisions of this section with the provisions of section 472.

(Added Pub. L. 96–223, title IV, § 403(a)(1), Apr. 2, 1980, 94 Stat. 302.)

EFFECTIVE DATE

Pub. L. 96–223, title IV, § 403(a)(3), Apr. 2, 1980, 94 Stat. 304, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that: ''The amendments made by paragraphs (1) and (2) [enacting this section] shall apply to qualified liquidations (within the meaning of section 473(c) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]) in taxable years ending after October 31, 1979.''

§ 474. Simplified dollar-value LIFO method for certain small businesses

(a) General rule

An eligible small business may elect to use the simplified dollar-value method of pricing inventories for purposes of the LIFO method.

(b) Simplified dollar-value method of pricing inventories

For purposes of this section—

(1) In general

The simplified dollar-value method of pricing inventories is a dollar-value method of pricing inventories under which—

(A) the taxpayer maintains a separate inventory pool for items in each major category in the applicable Government price index, and

(B) the adjustment for each such separate pool is based on the change from the preceding taxable year in the component of such index for the major category.

(2) Applicable Government price index

The term ''applicable Government price index'' means—

(A) except as provided in subparagraph (B), the Producer Price Index published by the Bureau of Labor Statistics, or

(B) in the case of a retailer using the retail method, the Consumer Price Index published by the Bureau of Labor Statistics.

(3) Major category

The term ''major category'' means—

(A) in the case of the Producer Price Index, any of the 2-digit standard industrial classifications in the Producer Prices Data Report, or

(B) in the case of the Consumer Price Index, any of the general expenditure categories in the Consumer Price Index Detailed Report.

(c) Eligible small business

For purposes of this section, a taxpayer is an eligible small business for any taxable year if the average annual gross receipts of the taxpayer for the 3 preceding taxable years do not exceed $5,000,000. For purposes of the preceding sentence, rules similar to the rules of section 448(c)(3) shall apply.

(d) Special rules

For purposes of this section—

(1) Controlled groups

(A) In general

In the case of a taxpayer which is a member of a controlled group, all persons which are component members of such group shall be treated as 1 taxpayer for purposes of determining the gross receipts of the taxpayer.

(B) Controlled group defined

For purposes of subparagraph (A), persons shall be treated as being component mem-

bers of a controlled group if such persons would be treated as a single employer under section 52.

(2) Election

(A) In general

The election under this section may be made without the consent of the Secretary.

(B) Period to which election applies

The election under this section shall apply—

(i) to the taxable year for which it is made, and

(ii) to all subsequent taxable years for which the taxpayer is an eligible small business,

unless the taxpayer secures the consent of the Secretary to the revocation of such election.

(3) LIFO method

The term ''LIFO method'' means the method provided by section 472(b).

(4) Transitional rules

(A) In general

In the case of a year of change under this section—

(i) the inventory pools shall—

(I) in the case of the 1st taxable year to which such an election applies, be established in accordance with the major categories in the applicable Government price index, or

(II) in the case of the 1st taxable year after such election ceases to apply, be established in the manner provided by regulations under section 472;

(ii) the aggregate dollar amount of the taxpayer's inventory as of the beginning of the year of change shall be the same as the aggregate dollar value as of the close of the taxable year preceding the year of change, and

(iii) the year of change shall be treated as a new base year in accordance with procedures provided by regulations under section 472.

(B) Year of change

For purposes of this paragraph, the year of change under this section is—

(i) the 1st taxable year to which an election under this section applies, or

(ii) in the case of a cessation of such an election, the 1st taxable year after such election ceases to apply.

(Added Pub. L. 97–34, title II, § 237(a), Aug. 13, 1981, 95 Stat. 252; amended Pub. L. 99–514, title VIII, § 802(a), Oct. 22, 1986, 100 Stat. 2348.)

AMENDMENTS

1986—Pub. L. 99–514 amended section generally, substituting provisions relating to election by eligible small business to use simplified dollar-value method of pricing inventories for purposes of LIFO method for provisions relating to election by eligible small business which uses dollar-value method of pricing inventories under method provided by section 472(b) of this title to use one inventory pool for any trade or business of such eligible small business.

EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99–514, title VIII, § 802(c), Oct. 22, 1986, 100 Stat. 2350, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1986.

''(2) TREATMENT OF TAXPAYERS WHO MADE ELECTIONS UNDER EXISTING SECTION 474.—The amendments made by this section shall not apply to any taxpayer who made an election under section 474 of the Internal Revenue Code of 1954 (as in effect on the day before the date of the enactment of this Act [Oct. 22, 1986]) for any period during which such election is in effect. Notwithstanding any provision of such section 474 (as so in effect), an election under such section may be revoked without the consent of the Secretary.''

EFFECTIVE DATE

Pub. L. 97–34, title II, § 237(c), Aug. 13, 1981, 95 Stat. 253, provided that: ''The amendments made by this section [enacting this section] shall apply to taxable years beginning after December 31, 1981.''

§ 475. Mark to market accounting method for dealers in securities

(a) General rule

Notwithstanding any other provision of this subpart, the following rules shall apply to securities held by a dealer in securities:

(1) Any security which is inventory in the hands of the dealer shall be included in inventory at its fair market value.

(2) In the case of any security which is not inventory in the hands of the dealer and which is held at the close of any taxable year—

(A) the dealer shall recognize gain or loss as if such security were sold for its fair market value on the last business day of such taxable year, and

(B) any gain or loss shall be taken into account for such taxable year.

Proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account under the preceding sentence. The Secretary may provide by regulations for the application of this paragraph at times other than the times provided in this paragraph.

(b) Exceptions

(1) In general

Subsection (a) shall not apply to—

(A) any security held for investment,

(B)(i) any security described in subsection (c)(2)(C) which is acquired (including originated) by the taxpayer in the ordinary course of a trade or business of the taxpayer and which is not held for sale, and (ii) any obligation to acquire a security described in clause (i) if such obligation is entered into in the ordinary course of such trade or business and is not held for sale, and

(C) any security which is a hedge with respect to—

(i) a security to which subsection (a) does not apply, or

(ii) a position, right to income, or a liability which is not a security in the hands of the taxpayer.

To the extent provided in regulations, subparagraph (C) shall not apply to any security

held by a person in its capacity as a dealer in securities.

(2) Identification required

A security shall not be treated as described in subparagraph (A), (B), or (C) of paragraph (1), as the case may be, unless such security is clearly identified in the dealer's records as being described in such subparagraph before the close of the day on which it was acquired, originated, or entered into (or such other time as the Secretary may by regulations prescribe).

(3) Securities subsequently not exempt

If a security ceases to be described in paragraph (1) at any time after it was identified as such under paragraph (2), subsection (a) shall apply to any changes in value of the security occurring after the cessation.

(4) Special rule for property held for investment

To the extent provided in regulations, subparagraph (A) of paragraph (1) shall not apply to any security described in subparagraph (D) or (E) of subsection (c)(2) which is held by a dealer in such securities.

(c) Definitions

For purposes of this section—

(1) Dealer in securities defined

The term ''dealer in securities'' means a taxpayer who—

(A) regularly purchases securities from or sells securities to customers in the ordinary course of a trade or business; or

(B) regularly offers to enter into, assume, offset, assign or otherwise terminate positions in securities with customers in the ordinary course of a trade or business.

(2) Security defined

The term ''security'' means any—

(A) share of stock in a corporation;

(B) partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust;

(C) note, bond, debenture, or other evidence of indebtedness;

(D) interest rate, currency, or equity notional principal contract;

(E) evidence of an interest in, or a derivative financial instrument in, any security described in subparagraph (A), (B), (C), or (D), or any currency, including any option, forward contract, short position, and any similar financial instrument in such a security or currency; and

(F) position which—

(i) is not a security described in subparagraph (A), (B), (C), (D), or (E),

(ii) is a hedge with respect to such a security, and

(iii) is clearly identified in the dealer's records as being described in this subparagraph before the close of the day on which it was acquired or entered into (or such other time as the Secretary may by regulations prescribe).

Subparagraph (E) shall not include any contract to which section 1256(a) applies.

(3) Hedge

The term ''hedge'' means any position which manages the dealer's risk of interest rate or price changes or currency fluctuations, including any position which is reasonably expected to become a hedge within 60 days after the acquisition of the position.

(4) Special rules for certain receivables

(A) In general

Paragraph (2)(C) shall not include any nonfinancial customer paper.

(B) Nonfinancial customer paper

For purposes of subparagraph (A), the term ''nonfinancial customer paper'' means any receivable which—

(i) is a note, bond, debenture, or other evidence of indebtedness;

(ii) arises out of the sale of nonfinancial goods or services by a person the principal activity of which is the selling or providing of nonfinancial goods or services; and

(iii) is held by such person (or a person who bears a relationship to such person described in section 267(b) or 707(b)) at all times since issue.

(d) Special rules

For purposes of this section—

(1) Coordination with certain rules

The rules of sections 263(g), 263A, and 1256(a) shall not apply to securities to which subsection (a) applies, and section 1091 shall not apply (and section 1092 shall apply) to any loss recognized under subsection (a).

(2) Improper identification

If a taxpayer—

(A) identifies any security under subsection (b)(2) as being described in subsection (b)(1) and such security is not so described, or

(B) fails under subsection (c)(2)(F)(iii) to identify any position which is described in subsection (c)(2)(F) (without regard to clause (iii) thereof) at the time such identification is required,

the provisions of subsection (a) shall apply to such security or position, except that any loss under this section prior to the disposition of the security or position shall be recognized only to the extent of gain previously recognized under this section (and not previously taken into account under this paragraph) with respect to such security or position.

(3) Character of gain or loss

(A) In general

Except as provided in subparagraph (B) or section 1236(b)—

(i) In general

Any gain or loss with respect to a security under subsection (a)(2) shall be treated as ordinary income or loss.

(ii) Special rule for dispositions

If—

(I) gain or loss is recognized with respect to a security before the close of the taxable year, and

(II) subsection (a)(2) would have applied if the security were held as of the close of the taxable year,

such gain or loss shall be treated as ordinary income or loss.

(B) Exception

Subparagraph (A) shall not apply to any gain or loss which is allocable to a period during which—

(i) the security is described in subsection (b)(1)(C) (without regard to subsection (b)(2)),

(ii) the security is held by a person other than in connection with its activities as a dealer in securities, or

(iii) the security is improperly identified (within the meaning of subparagraph (A) or (B) of paragraph (2)).

(e) Election of mark to market for dealers in commodities

(1) In general

In the case of a dealer in commodities who elects the application of this subsection, this section shall apply to commodities held by such dealer in the same manner as this section applies to securities held by a dealer in securities.

(2) Commodity

For purposes of this subsection and subsection (f), the term ''commodity'' means—

(A) any commodity which is actively traded (within the meaning of section 1092(d)(1));

(B) any notional principal contract with respect to any commodity described in subparagraph (A);

(C) any evidence of an interest in, or a derivative instrument in, any commodity described in subparagraph (A) or (B), including any option, forward contract, futures contract, short position, and any similar instrument in such a commodity; and

(D) any position which—

(i) is not a commodity described in subparagraph (A), (B), or (C),

(ii) is a hedge with respect to such a commodity, and

(iii) is clearly identified in the taxpayer's records as being described in this subparagraph before the close of the day on which it was acquired or entered into (or such other time as the Secretary may by regulations prescribe).

(3) Election

An election under this subsection may be made without the consent of the Secretary. Such an election, once made, shall apply to the taxable year for which made and all subsequent taxable years unless revoked with the consent of the Secretary.

(f) Election of mark to market for traders in securities or commodities

(1) Traders in securities

(A) In general

In the case of a person who is engaged in a trade or business as a trader in securities and who elects to have this paragraph apply to such trade or business—

(i) such person shall recognize gain or loss on any security held in connection with such trade or business at the close of any taxable year as if such security were sold for its fair market value on the last business day of such taxable year, and

(ii) any gain or loss shall be taken into account for such taxable year.

Proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account under the preceding sentence. The Secretary may provide by regulations for the application of this subparagraph at times other than the times provided in this subparagraph.

(B) Exception

Subparagraph (A) shall not apply to any security—

(i) which is established to the satisfaction of the Secretary as having no connection to the activities of such person as a trader, and

(ii) which is clearly identified in such person's records as being described in clause (i) before the close of the day on which it was acquired, originated, or entered into (or such other time as the Secretary may by regulations prescribe).

If a security ceases to be described in clause (i) at any time after it was identified as such under clause (ii), subparagraph (A) shall apply to any changes in value of the security occurring after the cessation.

(C) Coordination with section 1259

Any security to which subparagraph (A) applies and which was acquired in the normal course of the taxpayer's activities as a trader in securities shall not be taken into account in applying section 1259 to any position to which subparagraph (A) does not apply.

(D) Other rules to apply

Rules similar to the rules of subsections (b)(4) and (d) shall apply to securities held by a person in any trade or business with respect to which an election under this paragraph is in effect. Subsection (d)(3) shall not apply under the preceding sentence for purposes of applying sections 1402 and 7704.

(2) Traders in commodities

In the case of a person who is engaged in a trade or business as a trader in commodities and who elects to have this paragraph apply to such trade or business, paragraph (1) shall apply to commodities held by such trader in connection with such trade or business in the same manner as paragraph (1) applies to securities held by a trader in securities.

(3) Election

The elections under paragraphs (1) and (2) may be made separately for each trade or business and without the consent of the Secretary. Such an election, once made, shall apply to the taxable year for which made and all subsequent taxable years unless revoked with the consent of the Secretary.

(g) Regulatory authority

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including rules—

(1) to prevent the use of year-end transfers, related parties, or other arrangements to avoid the provisions of this section,

(2) to provide for the application of this section to any security which is a hedge which cannot be identified with a specific security, position, right to income, or liability, and

(3) to prevent the use by taxpayers of subsection (c)(4) to avoid the application of this section to a receivable that is inventory in the hands of the taxpayer (or a person who bears a relationship to the taxpayer described in section 267(b) or 707(b)).

(Added Pub. L. 103–66, title XIII, § 13223(a), Aug. 10, 1993, 107 Stat. 481; amended Pub. L. 105–34, title X, § 1001(b), Aug. 5, 1997, 111 Stat. 906; Pub. L. 105–206, title VI, § 6010(a)(3), title VII, § 7003(a), (b), July 22, 1998, 112 Stat. 813, 832; Pub. L. 106–170, title V, § 532(b)(1), Dec. 17, 1999, 113 Stat. 1930; Pub. L. 106–554, § 1(a)(7) [title III, § 319(4)], Dec. 21, 2000, 114 Stat. 2763, 2763A–646; Pub. L. 107–147, title IV, § 417(10), Mar. 9, 2002, 116 Stat. 56.)

AMENDMENTS

2002—Subsec. (g)(3). Pub. L. 107–147 substituted ''described in section'' for ''described in sections''.

2000—Subsec. (g)(3). Pub. L. 106–554 substituted ''267(b) or'' for ''267(b) of''.

1999—Subsec. (c)(3). Pub. L. 106–170 substituted ''manages'' for ''reduces''.

1998—Subsec. (c)(4). Pub. L. 105–206, § 7003(a), added par. (4).

Subsec. (f)(1)(D). Pub. L. 105–206, § 6010(a)(3), inserted at end ''Subsection (d)(3) shall not apply under the preceding sentence for purposes of applying sections 1402 and 7704.''

Subsec. (g)(3). Pub. L. 105–206, § 7003(b), added par. (3).

1997—Subsecs. (e) to (g). Pub. L. 105–34 added subsecs. (e) and (f) and redesignated former subsec. (e) as (g).

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106–170 applicable to any instrument held, acquired, or entered into, any transaction entered into, and supplies held or acquired on or after Dec. 17, 1999, see section 532(d) of Pub. L. 106–170, set out as a note under section 170 of this title.

EFFECTIVE DATE OF 1998 AMENDMENT

Amendment by section 6010(a)(3) of Pub. L. 105–206 effective, except as otherwise provided, as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105–34, to which such amendment relates, see section 6024 of Pub. L. 105–206, set out as a note under section 1 of this title.

Pub. L. 105–206, title VII, § 7003(c), July 22, 1998, 112 Stat. 833, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to taxable years ending after the date of the enactment of this Act [July 22, 1998].

''(2) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer required by the amendments made by this section to change its method of accounting for its first taxable year ending after the date of the enactment of this Act—

''(A) such change shall be treated as initiated by the taxpayer;

''(B) such change shall be treated as made with the consent of the Secretary of the Treasury; and

''(C) the net amount of the adjustments required to be taken into account by the taxpayer under section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the 4-taxable-year period beginning with such first taxable year.''

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105–34, title X, § 1001(d), Aug. 5, 1997, 111 Stat. 907, as amended by Pub. L. 105–206, title VI, § 6010(a)(4), July 22, 1998, 112 Stat. 813, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting section 1259 of this title and amending this section] shall apply to any constructive sale after June 8, 1997.

''(2) EXCEPTION FOR SALES OF POSITIONS, ETC. HELD BEFORE JUNE 9, 1997.—If—

''(A) before June 9, 1997, the taxpayer entered into any transaction which is a constructive sale of any appreciated financial position, and

''(B) before the close of the 30-day period beginning on the date of the enactment of this Act [Aug. 5, 1997] or before such later date as may be specified by the Secretary of the Treasury, such transaction and position are clearly identified in the taxpayer's records as offsetting,

such transaction and position shall not be taken into account in determining whether any other constructive sale after June 8, 1997, has occurred. The preceding sentence shall cease to apply as of the date such transaction is closed or the taxpayer ceases to hold such position.

''(3) SPECIAL RULE.—In the case of a decedent dying after June 8, 1997, if—

''(A) there was a constructive sale on or before such date of any appreciated financial position,

''(B) the transaction resulting in such constructive sale of such position remains open (with respect to the decedent or any related person)—

''(i) for not less than 2 years after the date of such transaction (whether such period is before or after June 8, 1997), and

''(ii) at any time during the 3-year period ending on the date of the decedent's death, and

''(C) such transaction is not closed before the close of the 30th day after the date of the enactment of this Act,

then, for purposes of such Code [probably means the Internal Revenue Code of 1986], such position (and the transaction resulting in such constructive sale) shall be treated as property constituting rights to receive an item of income in respect of a decedent under section 691 of such Code. Section 1014(c) of such Code shall not apply to so much of such position's or property's value (as included in the decedent's estate for purposes of chapter 11 of such Code) as exceeds its fair market value as of the date such transaction is closed.

''(4) ELECTION OF MARK TO MARKET BY SECURITIES TRADERS AND TRADERS AND DEALERS IN COMMODITIES.—

''(A) IN GENERAL.—The amendments made by subsection (b) [amending this section] shall apply to taxable years ending after the date of the enactment of this Act.

''(B) 4-YEAR SPREAD OF ADJUSTMENTS.—In the case of a taxpayer who elects under subsection (e) or (f) of section 475 of the Internal Revenue Code of 1986 (as added by this section) to change its method of accounting for the taxable year which includes the date of the enactment of this Act—

''(i) any identification required under such subsection with respect to securities and commodities held on the date of the enactment of this Act shall be treated as timely made if made on or before the 30th day after such date of enactment, and

''(ii) the net amount of the adjustments required to be taken into account by the taxpayer under section 481 of such Code shall be taken into account ratably over the 4-taxable year period beginning with such first taxable year.''

EFFECTIVE DATE

Pub. L. 103–66, title XIII, § 13223(c), Aug. 10, 1993, 107 Stat. 484, provided that:

''(1) IN GENERAL.—The amendments made by this section [enacting this section and amending section 988 of this title] shall apply to all taxable years ending on or after December 31, 1993.

''(2) CHANGE IN METHOD OF ACCOUNTING.—In the case of any taxpayer required by this section to change its method of accounting for any taxable year—

''(A) such change shall be treated as initiated by the taxpayer,

''(B) such change shall be treated as made with the consent of the Secretary, and

''(C) except as provided in paragraph (3), the net amount of the adjustments required to be taken into account by the taxpayer under section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the 5-taxable year period beginning with the first taxable year ending on or after December 31, 1993.

''(3) SPECIAL RULE FOR FLOOR SPECIALISTS AND MARKET MAKERS.—

''(A) IN GENERAL.—If—

''(i) a taxpayer (or any predecessor) used the last-in first-out (LIFO) method of accounting with respect to any qualified securities for the 5-taxable year period ending with its last taxable year ending before December 31, 1993, and

''(ii) any portion of the net amount described in paragraph (2)(C) is attributable to the use of such method of accounting,

then paragraph (2)(C) shall be applied by taking such portion into account ratably over the 15-taxable year period beginning with the first taxable year ending on or after December 31, 1993.

''(B) QUALIFIED SECURITY.—For purposes of this paragraph, the term 'qualified security' means any security acquired—

''(i) by a floor specialist (as defined in section 1236(d)(2) of the Internal Revenue Code of 1986) in connection with the specialist's duties as a specialist on an exchange, but only if the security is one in which the specialist is registered with the exchange, or

''(ii) by a taxpayer who is a market maker in connection with the taxpayer's duties as a market maker, but only if—

''(I) the security is included on the National Association of Security Dealers Automated Quotation System,

''(II) the taxpayer is registered as a market maker in such security with the National Association of Security Dealers, and

''(III) as of the last day of the taxable year preceding the taxpayer's first taxable year ending on or after December 31, 1993, the taxpayer (or any predecessor) has been actively and regularly engaged as a market maker in such security for the 2-year period ending on such date (or, if shorter, the period beginning 61 days after the security was listed in such quotation system and ending on such date).''

PART III—ADJUSTMENTS

AMENDMENTS

1964—Pub. L. 88–272, title II, §224(b), Feb. 26, 1964, 78 Stat. 79, added item 483.

§ 481. Adjustments required by changes in method of accounting

(a) General rule

In computing the taxpayer's taxable income for any taxable year (referred to in this section as the ''year of the change'')—

(1) if such computation is under a method of accounting different from the method under which the taxpayer's taxable income for the preceding taxable year was computed, then

(2) there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted, except there shall not be taken into account any adjustment in respect of any taxable year to which this section does not apply unless the adjustment is attributable to a change in the method of accounting initiated by the taxpayer.

(b) Limitation on tax where adjustments are substantial

(1) Three year allocation

If—

(A) the method of accounting from which the change is made was used by the taxpayer in computing his taxable income for the 2 taxable years preceding the year of the change, and

(B) the increase in taxable income for the year of the change which results solely by reason of the adjustments required by subsection (a)(2) exceeds $3,000,

then the tax under this chapter attributable to such increase in taxable income shall not be greater than the aggregate increase in the taxes under this chapter (or under the corresponding provisions of prior revenue laws) which would result if one-third of such increase in taxable income were included in taxable income for the year of the change and one-third of such increase were included for each of the 2 preceding taxable years.

(2) Allocation under new method of accounting

If—

(A) the increase in taxable income for the year of the change which results solely by reason of the adjustments required by subsection (a)(2) exceeds $3,000, and

(B) the taxpayer establishes his taxable income (under the new method of accounting) for one or more taxable years consecutively preceding the taxable year of the change for which the taxpayer in computing taxable income used the method of accounting from which the change is made,

then the tax under this chapter attributable to such increase in taxable income shall not be greater than the net increase in the taxes under this chapter (or under the corresponding provisions of prior revenue laws) which would result if the adjustments required by subsection (a)(2) were allocated to the taxable year or years specified in subparagraph (B) to which they are properly allocable under the new method of accounting and the balance of the adjustments required by subsection (a)(2) was allocated to the taxable year of the change.

(3) Special rules for computations under paragraphs (1) and (2)

For purposes of this subsection—

(A) There shall be taken into account the increase or decrease in tax for any taxable

year preceding the year of the change to which no adjustment is allocated under paragraph (1) or (2) but which is affected by a net operating loss (as defined in section 172) or by a capital loss carryback or carryover (as defined in section 1212), determined with reference to taxable years with respect to which adjustments under paragraph (1) or (2) are allocated.

(B) The increase or decrease in the tax for any taxable year for which an assessment of any deficiency, or a credit or refund of any overpayment, is prevented by any law or rule of law, shall be determined by reference to the tax previously determined (within the meaning of section 1314(a)) for such year.

(c) Adjustments under regulations

In the case of any change described in subsection (a), the taxpayer may, in such manner and subject to such conditions as the Secretary may by regulations prescribe, take the adjustments required by subsection (a)(2) into account in computing the tax imposed by this chapter for the taxable year or years permitted under such regulations.

(d) Adjustments attributable to conversion from S corporation to C corporation

(1) In general

In the case of an eligible terminated S corporation, any adjustment required by subsection (a)(2) which is attributable to such corporation's revocation described in paragraph (2)(A)(ii) shall be taken into account ratably during the 6-taxable year period beginning with the year of change.

(2) Eligible terminated S corporation

For purposes of this subsection, the term ''eligible terminated S corporation'' means any C corporation—

(A) which—

(i) was an S corporation on the day before the date of the enactment of the Tax Cuts and Jobs Act, and

(ii) during the 2-year period beginning on the date of such enactment makes a revocation of its election under section 1362(a), and

(B) the owners of the stock of which, determined on the date such revocation is made, are the same owners (and in identical proportions) as on the date of such enactment.

(Aug. 16, 1954, ch. 736, 68A Stat. 160; Pub. L. 85–866, title I, § 29(a), (b), Sept. 2, 1958, 72 Stat. 1626–1628; Pub. L. 91–172, title V, § 512(f)(4), Dec. 30, 1969, 83 Stat. 641; Pub. L. 94–455, title XIX, §§ 1901(a)(70), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1776, 1834; Pub. L. 96–471, § 2(b)(3), Oct. 19, 1980, 94 Stat. 2254; Pub. L. 113–295, div. A, title II, § 221(a)(61), Dec. 19, 2014, 128 Stat. 4048; Pub. L. 115–97, title I, § 13543(a), Dec. 22, 2017, 131 Stat. 2155.)

REFERENCES IN TEXT

The date of the enactment of the Tax Cuts and Jobs Act and the date of such enactment, referred to in subsec. (d)(2), probably mean the date of enactment of title I of Pub. L. 115–97, which was approved Dec. 22, 2017. Prior versions of the bill that was enacted into law as Pub. L. 115–97 included such Short Title, but it was not enacted as part of title I of Pub. L. 115–97.

AMENDMENTS

2017—Subsec. (d). Pub. L. 115–97 added subsec. (d).

2014—Subsec. (b)(3)(C). Pub. L. 113–295 struck out subpar. (C) which read as follows: ''In applying section 7807(b)(1), the provisions of chapter 1 (other than subchapter E, relating to self-employment income) and chapter 2 of the Internal Revenue Code of 1939 shall be treated as the corresponding provisions of the Internal Revenue Code of 1939.''

1980—Subsec. (d). Pub. L. 96–471 struck out subsec. (d) which provided that this section was not to apply to a change to which section 453 of this title, relating to change to installment method, applied.

1976—Subsecs. (b)(1), (2). Pub. L. 94–455, § 1901(a)(70)(B), struck out '', other than the amount of such adjustments to which paragraph (4) or (5) applies,'' after ''required by subsection (a)(2)''.

Subsec. (b)(4), (5), (6). Pub. L. 94–455, § 1901(a)(70)(A), struck out par. (4) which related to special rule for pre-1954 general adjustments, par. (5) which related to special rule for pre-1954 adjustments in case of certain decedents, and par. (6) which related to the application of the special rule for pre-1954 general adjustments.

Subsec. (c). Pub. L. 94–455, § 1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary''.

1969—Subsec. (b)(3)(A). Pub. L. 91–172 substituted ''loss carryback or carryover'' for ''loss carryover''.

1958—Subsec. (a)(2). Pub. L. 85–866, § 29(a)(1), inserted ''unless the adjustment is attributable to a change in the method of accounting initiated by the taxpayer'', after ''does not apply''.

Subsec. (b)(1). Pub. L. 85–866, § 29(b)(1)–(3), inserted '', other than the amount of such adjustments to which paragraph (4) or (5) applies,'' after ''subsection (a)(2)'' and substituted ''the aggregate increase in the taxes'' for ''the aggregate of the taxes'' and ''which would result if one-third of such increase in taxable income'' for ''which would result if one-third of such increase''.

Subsec. (b)(2). Pub. L. 85–866, § 29(b)(1), (4), inserted ''other than the amount of such adjustments to which paragraph (4) or (5) applies,'' after ''subsection (a)(2)'', wherever appearing and ''(or under the corresponding provisions of prior revenue laws)'' after ''the net increase in the taxes under this Chapter''.

Subsec. (b)(3)(A). Pub. L. 85–866, § 29(b)(5), substituted ''paragraph (1) or (2)'' for ''paragraph (2)'', wherever appearing.

Subsec. (b)(4) to (6). Pub. L. 85–866, § 29(a)(2), added pars. (4) to (6).

EFFECTIVE DATE OF 2014 AMENDMENT

Amendment by Pub. L. 113–295 effective Dec. 19, 2014, subject to a savings provision, see section 221(b) of Pub. L. 113–295, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1980 AMENDMENT

For effective date of amendment by Pub. L. 96–471, see section 6(a)(1) of Pub. L. 96–471, set out as an Effective Date note under section 453 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(70) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

EFFECTIVE DATE OF 1969 AMENDMENT

Amendment by Pub. L. 91–172 applicable with respect to net capital losses sustained in taxable years beginning after Dec. 31, 1969, see section 512(g) of Pub. L. 91–172, set out as a note under section 1212 of this title.

EFFECTIVE DATE OF 1958 AMENDMENT

Pub. L. 85–866, title I, § 29(d), Sept. 2, 1958, 72 Stat. 1629, as amended by Pub. L. 99–514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

''(1) IN GENERAL.—The amendments made by this section [amending this section and section 381 of this title] shall apply with respect to any change in a method of accounting where the year of the change (within the meaning of section 481 of the Internal Revenue Code of 1986 [formerly I.R.C. 1954]) is a taxable year beginning after December 31, 1953, and ending after August 16, 1954.

''(2) EXCEPTION FOR CERTAIN AGREEMENTS.—The amendments made by subsections (a), (b)(I), and (c) [amending this section and section 381 of this title] shall not apply if before the date of the enactment of this Act [Sept. 2, 1958]—

''(A) the taxpayer applied for a change in the method of accounting in the manner provided by regulations prescribed by the Secretary of the Treasury or his delegate, and

''(B) the taxpayer and the Secretary of the Treasury or his delegate agreed to the terms and conditions for making the change.''

CHANGES IN TREATMENT OF POLICYHOLDER DIVIDENDS BY QUALIFIED GROUP SELF-INSURERS' FUNDS

Pub. L. 101–239, title VII, §7816(m), Dec. 19, 1989, 103 Stat. 2421, provided that: ''If, for the 1st taxable year beginning on or after January 1, 1987, a qualified group self-insurers' fund changes its treatment of policyholder dividends to take into account such dividends no earlier than the date that the State regulatory authority determines the amount of the policyholder dividend that may be paid, then such change shall be treated as a change in a method of accounting and no adjustment under section 481(a) of the Internal Revenue Code of 1986 shall be made with respect to such change in method of accounting.''

TRANSITIONAL PROVISIONS FOR INCOME TAX TREATMENT OF DEALER RESERVE INCOME

Pub. L. 86–459, May 13, 1960, 74 Stat. 124, authorized any person who computed taxable income under the accrual method of accounting for his most recent taxable year ending on or before June 22, 1959, and who treated dealer reserve income for such taxable year as accruable for a subsequent taxable year, to elect before Sept. 1, 1960, to have section 481 of this title apply to the treatment for income tax purposes of dealer reserve income.

ELECTION TO RETURN TO FORMER METHOD OF ACCOUNTING

Pub. L. 85–866, title I, §29(e), Sept. 2, 1958, 72 Stat. 1629, authorized an election by certain taxpayers, who, for any taxable years beginning after Dec. 31, 1953, and ending after Aug. 16, 1954, and before Sept. 2, 1958, computed their taxable incomes using different accounting methods in succeeding taxable years, to return to their first method of accounting, where the election was made within six months after Sept. 2, 1958. Claims for refunds of overpayments of tax resulting from the election were to be filed within one year after the date of the election. Such an election was to be considered a consent to an assessment of a deficiency resulting from the election, where the assessment is made within one year after the date of the election.

§ 482. Allocation of income and deductions among taxpayers

In any case of two or more organizations, trades, or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the Secretary may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades, or businesses. In the case of any transfer (or license) of intangible property (within the meaning of section 367(d)(4)), the income with respect to such transfer or license shall be commensurate with the income attributable to the intangible. For purposes of this section, the Secretary shall require the valuation of transfers of intangible property (including intangible property transferred with other property or services) on an aggregate basis or the valuation of such a transfer on the basis of the realistic alternatives to such a transfer, if the Secretary determines that such basis is the most reliable means of valuation of such transfers.

(Aug. 16, 1954, ch. 736, 68A Stat. 162; Pub. L. 94–455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 99–514, title XII, §1231(e)(1), Oct. 22, 1986, 100 Stat. 2562; Pub. L. 115–97, title I, §14221(b)(2), Dec. 22, 2017, 131 Stat. 2219; Pub. L. 115–141, div. U, title IV, §401(d)(1)(D)(viii)(III), Mar. 23, 2018, 132 Stat. 1207.)

AMENDMENTS

2018—Pub. L. 115–141 substituted ''section 367(d)(4)'' for ''section 936(h)(3)(B)''.

2017—Pub. L. 115–97 inserted at end ''For purposes of this section, the Secretary shall require the valuation of transfers of intangible property (including intangible property transferred with other property or services) on an aggregate basis or the valuation of such a transfer on the basis of the realistic alternatives to such a transfer, if the Secretary determines that such basis is the most reliable means of valuation of such transfers.''

1986—Pub. L. 99–514 inserted at end ''In the case of any transfer (or license) of intangible property (within the meaning of section 936(h)(3)(B)), the income with respect to such transfer or license shall be commensurate with the income attributable to the intangible.''

1976—Pub. L. 94–455 struck out ''or his delegate'' after ''Secretary''.

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by Pub. L. 115–97 applicable to transfers in taxable years beginning after Dec. 31, 2017, see section 14221(c)(1) of Pub. L. 115–97, set out as a note under section 367 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99–514 applicable to taxable years beginning after Dec. 31, 1986, but only with respect to transfers after Nov. 16, 1985, or licenses granted after such date, or before such date with respect to property not in existence or owned by the taxpayer on such date, except that for purposes of [former] section 936(h)(5)(C) of this title, such amendment applicable to taxable years beginning after Dec. 31, 1986, without regard to when the transfer or license was made, see section 1231(g)(2) of Pub. L. 99–514, set out as a note under section 367 of this title.

REGULATIONS

For requirement that, not later than 180 days after July 18, 1984, the Secretary of the Treasury modify the safe harbor interest rates applicable under the regulations prescribed under this section so that such rates are consistent with the rates applicable under section 483 of this title by reason of the amendments made by Pub. L. 98–369, see section 44(b)(2) of Pub. L. 98–369, set out as an Effective Date note under section 1271 of this title.

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 115–141 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Mar. 23, 2018, for purposes of determining liability for tax for periods ending after Mar. 23, 2018, see section 401(e) of Pub. L. 115–141, set out as a note under section 23 of this title.

STUDY OF APPLICATION AND ADMINISTRATION OF THIS SECTION

Pub. L. 101–508, title XI, § 11316, Nov. 5, 1990, 104 Stat. 1388–458, directed Secretary of the Treasury or his delegate to conduct a study of the application and administration of section 482 of the Internal Revenue Code of 1986 and not later than Mar. 1, 1992, submit to Committee on Ways and Means of House of Representatives and Committee on Finance of Senate a report on the study, together with such recommendations as he deemed advisable.

§ 483. Interest on certain deferred payments

(a) Amount constituting interest

For purposes of this title, in the case of any payment—

(1) under any contract for the sale or exchange of any property, and

(2) to which this section applies,

there shall be treated as interest that portion of the total unstated interest under such contract which, as determined in a manner consistent with the method of computing interest under section 1272(a), is properly allocable to such payment.

(b) Total unstated interest

For purposes of this section, the term ''total unstated interest'' means, with respect to a contract for the sale or exchange of property, an amount equal to the excess of—

(1) the sum of the payments to which this section applies which are due under the contract, over

(2) the sum of the present values of such payments and the present values of any interest payments due under the contract.

For purposes of the preceding sentence, the present value of a payment shall be determined under the rules of section 1274(b)(2) using a discount rate equal to the applicable Federal rate determined under section 1274(d).

(c) Payments to which subsection (a) applies

(1) In general

Except as provided in subsection (d), this section shall apply to any payment on account of the sale or exchange of property which constitutes part or all of the sales price and which is due more than 6 months after the date of such sale or exchange under a contract—

(A) under which some or all of the payments are due more than 1 year after the date of such sale or exchange, and

(B) under which there is total unstated interest.

(2) Treatment of other debt instruments

For purposes of this section, a debt instrument of the purchaser which is given in consideration for the sale or exchange of property shall not be treated as a payment, and any payment due under such debt instrument shall be treated as due under the contract for the sale or exchange.

(3) Debt instrument defined

For purposes of this subsection, the term ''debt instrument'' has the meaning given such term by section 1275(a)(1).

(d) Exceptions and limitations

(1) Coordination with original issue discount rules

This section shall not apply to any debt instrument for which an issue price is determined under section 1273(b) (other than paragraph (4) thereof) or section 1274.

(2) Sales prices of $3,000 or less

This section shall not apply to any payment on account of the sale or exchange of property if it can be determined at the time of such sale or exchange that the sales price cannot exceed $3,000.

(3) Carrying charges

In the case of the purchaser, the tax treatment of amounts paid on account of the sale or exchange of property shall be made without regard to this section if any such amounts are treated under section 163(b) as if they included interest.

(4) Certain sales of patents

In the case of any transfer described in section 1235(a) (relating to sale or exchange of patents), this section shall not apply to any amount contingent on the productivity, use, or disposition of the property transferred.

(e) Maximum rate of interest on certain transfers of land between related parties

(1) In general

In the case of any qualified sale, the discount rate used in determining the total unstated interest rate under subsection (b) shall not exceed 6 percent, compounded semiannually.

(2) Qualified sale

For purposes of this subsection, the term ''qualified sale'' means any sale or exchange of land by an individual to a member of such individual's family (within the meaning of section 267(c)(4)).

(3) $500,000 limitation

Paragraph (1) shall not apply to any qualified sale between individuals made during any calendar year to the extent that the sales price for such sale (when added to the aggregate sales price for prior qualified sales between such individuals during the calendar year) exceeds $500,000.

(4) Nonresident alien individuals

Paragraph (1) shall not apply to any sale or exchange if any party to such sale or exchange is a nonresident alien individual.

(f) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section including regulations providing for the application of this section in the case of—

(1) any contract for the sale or exchange of property under which the liability for, or the amount or due date of, a payment cannot be determined at the time of the sale or exchange, or

(2) any change in the liability for, or the amount or due date of, any payment (including interest) under a contract for the sale or exchange of property.

(g) Cross references

(1) For treatment of assumptions, see section l274(c)(4).

(2) For special rules for certain transactions where stated principal amount does not exceed $2,800,000, see section 1274A.

(3) For special rules in case of the borrower under certain loans for personal use, see section 1275(b).

(Added Pub. L. 88–272, title II, §224(a), Feb. 26, 1964, 78 Stat. 77; amended Pub. L. 94–455, title XIX, §§1901(b)(3)(B), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1792, 1834; Pub. L. 97–34, title I, §126(a), Aug. 13, 1981, 95 Stat. 202; Pub. L. 97–448, title I, §101(g), Jan. 12, 1983, 96 Stat. 2367; Pub. L. 98–369, div. A, title I, §41(b), July 18, 1984, 98 Stat. 553; Pub. L. 99–121, title I, §§101(a)(2), 102(c)(1)–(3), Oct. 11, 1985, 99 Stat. 505, 508; Pub. L. 99–514, title XVIII, §1803(a)(14)(B), Oct. 22, 1986, 100 Stat. 2797.)

AMENDMENTS

1986—Subsec. (d)(3). Pub. L. 99–514 substituted ''for which an issue price is determined under section 1273(b) (other than paragraph (4) thereof) or section 1274'' for ''to which section 1272 applies''.

1985—Subsec. (b). Pub. L. 99–121, §101(a)(2)(A), struck out ''120 percent of'' after ''discount rate equal to'' in closing provisions.

Subsec. (c)(1)(B). Pub. L. 99–121, §101(a)(2)(B), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: ''under which, using a discount rate equal to 110 percent of the applicable Federal rate determined under section 1274(d), there is total unstated interest.''

Subsec. (e). Pub. L. 99–121, §102(c)(1), (2), redesignated subsec. (f) as (e), and as so redesignated substituted ''6 percent'' for ''7 percent'' in par. (1). Former subsec. (e), which related to the interest rates in the case of the sales of principal residences or farm lands, was struck out.

Subsec. (f). Pub. L. 99–121, §102(c)(1), redesignated subsec. (g) as (f). Former subsec. (f) redesignated (e).

Subsecs. (g), (h). Pub. L. 99–121, §102(c)(1), (3), redesignated subsec. (h) as (g) and amended it generally, designating existing undesignated cross reference as par. (3), and adding pars. (1) and (2). Former subsec. (g) redesignated (f).

1984—Subsec. (a). Pub. L. 98–369 amended subsec. (a) generally, substituting ''For purposes of this title, in the case of any payment (1) under any contract for the sale or exchange of any property, and (2) to which this section applies, there shall be treated as interest that portion of the total unstated interest under such contract which, as determined in a manner consistent with the method of computing interest under section 1272(a), is properly allocable to such payment'' for ''For purposes of this title, in the case of any contract for the sale or exchange of property there shall be treated as interest that part of a payment to which this section applies which bears the same ratio to the amount of such payment as the total unstated interest under such contract bears to the total of the payments to which this section applies which are due under such contract''.

Subsec. (b). Pub. L. 98–369 amended subsec. (b) generally, substituting provisions directing that the present value of a payment be determined under the rules of section 1274(b)(2) using a discount rate equal to 120 percent of the applicable Federal rate determined under section 1274(d) for provisions which had directed that the present value of a payment be determined, as of the date of the sale or exchange, by discounting such payment at the rate, and in the manner, provided in regulations prescribed by the Secretary and that such regulations provide for discounting on the basis of 6-month brackets and provide that the present value of any interest payment due not more than 6 months after the date of the sale or exchange was to have been an amount equal to 100 percent of such payment.

Subsec. (c). Pub. L. 98–369 substituted ''subsection (a) applies'' for ''section applies'' in heading.

Subsec. (c)(1). Pub. L. 98–369 substituted ''under which, using a discount rate equal to 110 percent of the applicable Federal rate determined under section 1274(d), there is total unstated interest'' for ''under which, using a rate provided by regulations prescribed by the Secretary for purposes of this subparagraph, there is total unstated interest'', in subpar. (B), and struck out provision formerly set out following subpar. (B) which had directed that any rate prescribed for determining whether there was total unstated interest for purposes of subpar. (B) be at least one percentage point lower than the rate prescribed for purposes of subsec. (b)(2).

Subsec. (c)(2). Pub. L. 98–369 substituted ''Treatment of other debt instruments'' for ''Treatment of other evidence of indebtedness'' in heading and, in text, substituted ''a debt instrument of the purchaser which is given in consideration for the sale or exchange of property shall not be treated as a payment, and any payment due under such debt instrument'' for ''an evidence of indebtedness of the purchaser given in consideration for the sale or exchange of property shall not be considered a payment, and any payment due under such evidence of indebtedness''.

Subsec. (c)(3). Pub. L. 98–369 added par. (3).

Subsec. (d). Pub. L. 98–369 amended subsec. (d) generally, substituting provisions relating to exceptions and limitations for provisions which related to payments indefinite as to time, liability, or amount.

Subsec. (e). Pub. L. 98–369 amended subsec. (e) generally, substituting provisions relating to interest rates in case of sale of principal residence or farm land for provision relating to changes in terms of contract.

Subsec. (f). Pub. L. 98–369 amended subsec. (f) generally, substituting provisions relating to maximum rate of interest on certain transfers of land between related parties for provisions which related to exceptions and limitations now covered in subsec. (d) of this section.

Subsec. (g). Pub. L. 98–369 amended subsec. (g) generally, substituting provisions which related to calling for the promulgation of regulations by the Secretary for provisions which related to the maximum rate of interest on certain transfers of land between related parties now covered in subsec. (f) of this section.

Subsec. (h). Pub. L. 98–369 added subsec. (h).

1983—Subsec. (g)(4). Pub. L. 97–448 substituted ''Paragraph (1)'' for ''This section''.

1981—Subsec. (g). Pub. L. 97–34 added subsec. (g).

1976—Subsecs. (b), (c)(1)(B), (e). Pub. L. 94–455, §1906(b)(13)(A), struck out ''or his delegate'' after ''Secretary''.

Subsec. (f)(3). Pub. L. 94–455, §1901(b)(3)(B), substituted ''all of the gain, if any, on such'' for ''no part of any gain on such'' and ''ordinary income'' for gain from the sale or exchange of property other than a capital asset''.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99–514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98–369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99–514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1985 AMENDMENT

Amendment by Pub. L. 99–121 applicable to sales and exchanges after June 30, 1985, in taxable years ending

after such date, see section 105(a)(1) of Pub. L. 99–121, set out as a note under section 1274 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98–369 applicable to taxable years ending after July 18, 1984, and applicable to sales or exchanges after Dec. 31, 1984, but not applicable to any sale or exchange pursuant to a written contract which was binding on Mar. 1, 1984, and at all times thereafter before the sale or exchange, see section 44 of Pub. L. 98–369, set out as an Effective Date note under section 1271 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97–448 effective, except as otherwise provided, as if it had been included in the provision of the Economic Recovery Tax Act of 1981, Pub. L. 97–34, to which such amendment relates, see section 109 of Pub. L. 97–448, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1981 AMENDMENT

Pub. L. 97–34, title I, § 126(b), Aug. 13, 1981, 95 Stat. 202, provided that: ''The amendment made by subsection (a) [amending this section] shall apply to payments made after June 30, 1981, pursuant to sales or exchanges after such date.''

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(b)(3)(B) of Pub. L. 94–455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94–455, set out as a note under section 2 of this title.

EFFECTIVE DATE

Section applicable to payments made after Dec. 31, 1963, on account of sales or exchanges of property after June 30, 1963, other than a sale or exchange pursuant to written contract, including an irrevocable written option, entered into before July 1, 1963, see section 224(d) of Pub. L. 88–272, set out as an Effective Date of 1964 Amendment note under section 163 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

TREATMENT OF TRANSFERS OF LAND BETWEEN RELATED PARTIES

Pub. L. 99–514, title XVIII, § 1803(a)(9), Oct. 22, 1986, 100 Stat. 2794, provided that: ''In the case of any sale or exchange before July 1, 1985, to which section 483(f) of the Internal Revenue Code of 1954 [now 1986] (as in effect on the day before the date of the enactment of Public Law 99–121 [Oct. 11, 1985]) applies, such section shall be treated as providing that the discount rate to be used for purposes of section 483(c)(1) of such Code shall be 6 percent, compounded semiannually.''

TRANSITIONAL RULE FOR PURPOSES OF IMPUTED INTEREST RULES

Provisions, respecting treatment of debt instruments received in exchange for property, relating to special rules for sales after Dec. 31, 1984, and before July 1, 1985, general rule for assumptions of loans, exception for assumptions of loans made on or before Oct. 15, 1984, and exception for assumptions of loans with respect to certain property, see section 44(b)(4)–(7) of Pub. L. 98–369, as amended, set out as an Effective Date note under section 1271 of this title.

Subchapter F—Exempt Organizations

AMENDMENTS

2018—Pub. L. 115–141, div. U, title IV, § 401(a)(121), Mar. 23, 2018, 132 Stat. 1190, substituted ''Certain Savings Entities'' for ''Certain Savings Entities.'' in part VIII heading.

2014—Pub. L. 113–295, div. B, title I, § 102(e)(5), Dec. 19, 2014, 128 Stat. 4062, substituted ''Certain Savings Entities'' for ''Higher education savings entities'' in part VIII heading.

1997—Pub. L. 105–34, title II, § 211(e)(1)(B), Aug. 5, 1997, 111 Stat. 812, substituted ''Higher education savings entities'' for ''Qualified State tuition programs'' in part VIII heading.

1996—Pub. L. 104–188, title I, § 1806(b)(2), Aug. 20, 1996, 110 Stat. 1898, added part VIII heading.

1976—Pub. L. 94–455, title XXI, § 2101(d), Oct. 4, 1976, 90 Stat. 1899, added part VII heading.

1975—Pub. L. 93–625, § 10(d), Jan. 3, 1975, 88 Stat. 2119, added part VI heading.

1969—Pub. L. 91–172, title I, § 101(j)(58), Dec. 30, 1969, 83 Stat. 532, added part II heading, and redesignated former parts II, III and IV as parts III, IV and V, respectively.

PART I—GENERAL RULE

AMENDMENTS

2018—Pub. L. 115–141, div. U, title IV, § 401(b)(21)(I), Mar. 23, 2018, 132 Stat. 1203, substituted ''Additional requirements for organizations described in paragraph (9) or (17) of section 501(c)'' for ''Additional requirements for organizations described in paragraph (9), (17), or (20) of section 501(c)'' in item 505.

2015—Pub. L. 114–113, div. Q, title IV, § 405(d), Dec. 18, 2015, 129 Stat. 3119, added item 506.

1987—Pub. L. 100–203, title X, § 10711(b)(2)(B), Dec. 22, 1987, 101 Stat. 1330–464, substituted ''substantial lobbying or because of political activities'' for ''substantial lobbying'' in item 504.

1984—Pub. L. 98–369, div. A, title V, § 513(b), July 18, 1984, 98 Stat. 865, added item 505.

1976—Pub. L. 94–455, title XIII, § 1307(d)(3)(B), Oct. 4, 1976, 90 Stat. 1728, added item 504.

1969—Pub. L. 91–172, title I, § 101(j)(61), Dec. 30, 1969, 83 Stat. 532, struck out item 504 ''Denial of exemption''.

§ 501. Exemption from tax on corporations, certain trusts, etc.

(a) Exemption from taxation

An organization described in subsection (c) or (d) or section 401(a) shall be exempt from tax-

[1] So in original. Probably should be ''Certain savings entities.''