

Pub. L. 108-357, set out as a note under section 246 of this title.

EFFECTIVE DATE

Pub. L. 103-66, title XIII, §13206(a)(3), Aug. 10, 1993, 107 Stat. 465, as amended by Pub. L. 104-188, title I, §1703(n)(11), Aug. 20, 1996, 110 Stat. 1877, provided that: "The amendments made by this subsection [enacting this section] shall apply to conversion transactions entered into after April 30, 1993."

§ 1259. Constructive sales treatment for appreciated financial positions

(a) In general

If there is a constructive sale of an appreciated financial position—

(1) the taxpayer shall recognize gain as if such position were sold, assigned, or otherwise terminated at its fair market value on the date of such constructive sale (and any gain shall be taken into account for the taxable year which includes such date), and

(2) for purposes of applying this title for periods after the constructive sale—

(A) proper adjustment shall be made in the amount of any gain or loss subsequently realized with respect to such position for any gain taken into account by reason of paragraph (1), and

(B) the holding period of such position shall be determined as if such position were originally acquired on the date of such constructive sale.

(b) Appreciated financial position

For purposes of this section—

(1) In general

Except as provided in paragraph (2), the term "appreciated financial position" means any position with respect to any stock, debt instrument, or partnership interest if there would be gain were such position sold, assigned, or otherwise terminated at its fair market value.

(2) Exceptions

The term "appreciated financial position" shall not include—

(A) any position with respect to debt if—

(i) the position unconditionally entitles the holder to receive a specified principal amount,

(ii) the interest payments (or other similar amounts) with respect to such position meet the requirements of clause (i) of section 860G(a)(1)(B), and

(iii) such position is not convertible (directly or indirectly) into stock of the issuer or any related person,

(B) any hedge with respect to a position described in subparagraph (A), and

(C) any position which is marked to market under any provision of this title or the regulations thereunder.

(3) Position

The term "position" means an interest, including a futures or forward contract, short sale, or option.

(c) Constructive sale

For purposes of this section—

(1) In general

A taxpayer shall be treated as having made a constructive sale of an appreciated financial position if the taxpayer (or a related person)—

(A) enters into a short sale of the same or substantially identical property,

(B) enters into an offsetting notional principal contract with respect to the same or substantially identical property,

(C) enters into a futures or forward contract to deliver the same or substantially identical property,

(D) in the case of an appreciated financial position that is a short sale or a contract described in subparagraph (B) or (C) with respect to any property, acquires the same or substantially identical property, or

(E) to the extent prescribed by the Secretary in regulations, enters into 1 or more other transactions (or acquires 1 or more positions) that have substantially the same effect as a transaction described in any of the preceding subparagraphs.

(2) Exception for sales of nonpublicly traded property

A taxpayer shall not be treated as having made a constructive sale solely because the taxpayer enters into a contract for sale of any stock, debt instrument, or partnership interest which is not a marketable security (as defined in section 453(f)) if the contract settles within 1 year after the date such contract is entered into.

(3) Exception for certain closed transactions

(A) In general

In applying this section, there shall be disregarded any transaction (which would otherwise cause a constructive sale) during the taxable year if—

(i) such transaction is closed on or before the 30th day after the close of such taxable year,

(ii) the taxpayer holds the appreciated financial position throughout the 60-day period beginning on the date such transaction is closed, and

(iii) at no time during such 60-day period is the taxpayer's risk of loss with respect to such position reduced by reason of a circumstance which would be described in section 246(c)(4) if references to stock included references to such position.

(B) Treatment of certain closed transactions where risk of loss on appreciated financial position diminished

If—

(i) a transaction, which would otherwise cause a constructive sale of an appreciated financial position, is closed during the taxable year or during the 30 days thereafter, and

(ii) another transaction is entered into during the 60-day period beginning on the date the transaction referred to in clause (i) is closed—

(I) which would (but for this subparagraph) cause the requirement of subparagraph (A)(iii) not to be met with respect

to the transaction described in clause (i) of this subparagraph,

(II) which is closed on or before the 30th day after the close of the taxable year in which the transaction referred to in clause (i) occurs, and

(III) which meets the requirements of clauses (ii) and (iii) of subparagraph (A),

the transaction referred to in clause (ii) shall be disregarded for purposes of determining whether the requirements of subparagraph (A)(iii) are met with respect to the transaction described in clause (i).

(4) Related person

A person is related to another person with respect to a transaction if—

(A) the relationship is described in section 267(b) or 707(b), and

(B) such transaction is entered into with a view toward avoiding the purposes of this section.

(d) Other definitions

For purposes of this section—

(1) Forward contract

The term “forward contract” means a contract to deliver a substantially fixed amount of property (including cash) for a substantially fixed price.

(2) Offsetting notional principal contract

The term “offsetting notional principal contract” means, with respect to any property, an agreement which includes—

(A) a requirement to pay (or provide credit for) all or substantially all of the investment yield (including appreciation) on such property for a specified period, and

(B) a right to be reimbursed for (or receive credit for) all or substantially all of any decline in the value of such property.

(e) Special rules

(1) Treatment of subsequent sale of position which was deemed sold

If—

(A) there is a constructive sale of any appreciated financial position,

(B) such position is subsequently disposed of, and

(C) at the time of such disposition, the transaction resulting in the constructive sale of such position is open with respect to the taxpayer or any related person,

solely for purposes of determining whether the taxpayer has entered into a constructive sale of any other appreciated financial position held by the taxpayer, the taxpayer shall be treated as entering into such transaction immediately after such disposition. For purposes of the preceding sentence, an assignment or other termination shall be treated as a disposition.

(2) Certain trust instruments treated as stock

For purposes of this section, an interest in a trust which is actively traded (within the meaning of section 1092(d)(1)) shall be treated as stock unless substantially all (by value) of the property held by the trust is debt described in subsection (b)(2)(A).

(3) Multiple positions in property

If a taxpayer holds multiple positions in property, the determination of whether a specific transaction is a constructive sale and, if so, which appreciated financial position is deemed sold shall be made in the same manner as actual sales.

(f) Regulations

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

(Added Pub. L. 105-34, title X, §1001(a), Aug. 5, 1997, 111 Stat. 903; amended Pub. L. 105-206, title VI, §6010(a)(1), (2), July 22, 1998, 112 Stat. 812, 813; Pub. L. 108-311, title IV, §406(e), Oct. 4, 2004, 118 Stat. 1189.)

Editorial Notes

AMENDMENTS

2004—Subsec. (c)(2). Pub. L. 108-311, §406(e)(1), substituted “A taxpayer shall not be treated as having made a constructive sale solely because the taxpayer enters into a contract” for “The term ‘constructive sale’ shall not include any contract”.

Subsec. (c)(3)(A). Pub. L. 108-311, §406(e)(2), substituted “cause a constructive sale” for “be treated as a constructive sale” in introductory provisions.

Subsec. (c)(3)(A)(i). Pub. L. 108-311, §406(e)(3), substituted “on or before” for “before the end of”.

Subsec. (c)(3)(B). Pub. L. 108-311, §406(e)(7), substituted “certain closed transactions where risk of loss on appreciated financial position diminished” for “positions which are reestablished” in heading.

Subsec. (c)(3)(B)(i). Pub. L. 108-311, §406(e)(2), substituted “cause a constructive sale” for “be treated as a constructive sale”.

Subsec. (c)(3)(B)(ii). Pub. L. 108-311, §406(e)(4), struck out “substantially similar” after “another” in introductory provisions.

Subsec. (c)(3)(B)(ii)(I). Pub. L. 108-311, §406(e)(5), amended subcl. (I) generally. Prior to amendment, subcl. (I) read as follows: “which also would otherwise be treated as a constructive sale of such position.”

Subsec. (c)(3)(B)(ii)(II). Pub. L. 108-311, §406(e)(6), inserted “on or” before “before the 30th day”.

1998—Subsec. (b)(2)(A)(i) to (iii). Pub. L. 105-206, §6010(a)(1)(A), substituted “position” for “debt”.

Subsec. (b)(2)(B), (C). Pub. L. 105-206, §6010(a)(1)(B), (C), added subpar. (B) and redesignated former subpar. (B) as (C).

Subsec. (d)(1). Pub. L. 105-206, §6010(a)(2), inserted “(including cash)” after “property”.

Statutory Notes and Related Subsidiaries

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-311 effective as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 406(h) of Pub. L. 108-311, set out as a note under section 55 of this title.

EFFECTIVE DATE OF 1998 AMENDMENT

Amendment by 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.

EFFECTIVE DATE

Section applicable to any constructive sale after June 8, 1997, with certain exceptions, see section 1001(d) of Pub. L. 105-34, set out as an Effective Date of 1997 Amendment note under section 475 of this title.

§ 1260. Gains from constructive ownership transactions**(a) In general**

If the taxpayer has gain from a constructive ownership transaction with respect to any financial asset and such gain would (without regard to this section) be treated as a long-term capital gain—

(1) such gain shall be treated as ordinary income to the extent that such gain exceeds the net underlying long-term capital gain, and

(2) to the extent such gain is treated as a long-term capital gain after the application of paragraph (1), the determination of the capital gain rate (or rates) applicable to such gain under section 1(h) shall be determined on the basis of the respective rate (or rates) that would have been applicable to the net underlying long-term capital gain.

(b) Interest charge on deferral of gain recognition**(1) In general**

If any gain is treated as ordinary income for any taxable year by reason of subsection (a)(1), the tax imposed by this chapter for such taxable year shall be increased by the amount of interest determined under paragraph (2) with respect to each prior taxable year during any portion of which the constructive ownership transaction was open. 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.

(2) Amount of interest

The amount of interest determined under this paragraph with respect to a prior taxable year is the amount of interest which would have been imposed under section 6601 on the underpayment of tax for such year which would have resulted if the gain (which is treated as ordinary income by reason of subsection (a)(1)) had been included in gross income in the taxable years in which it accrued (determined by treating the income as accruing at a constant rate equal to the applicable Federal rate as in effect on the day the transaction closed). The period during which such interest shall accrue shall end on the due date (without extensions) for the return of tax imposed by this chapter for the taxable year in which such transaction closed.

(3) Applicable Federal rate

For purposes of paragraph (2), the applicable Federal rate is the applicable Federal rate determined under section 1274(d) (compounded semiannually) which would apply to a debt instrument with a term equal to the period the transaction was open.

(4) No credits against increase in tax

Any increase in tax under paragraph (1) shall not be treated as tax imposed by this chapter for purposes of determining—

(A) the amount of any credit allowable under this chapter, or

(B) the amount of the tax imposed by section 55.

(c) Financial asset

For purposes of this section—

(1) In general

The term “financial asset” means—

(A) any equity interest in any pass-thru entity, and

(B) to the extent provided in regulations—

(i) any debt instrument, and

(ii) any stock in a corporation which is not a pass-thru entity.

(2) Pass-thru entity

For purposes of paragraph (1), the term “pass-thru entity” means—

(A) a regulated investment company,

(B) a real estate investment trust,

(C) an S corporation,

(D) a partnership,

(E) a trust,

(F) a common trust fund,

(G) a passive foreign investment company (as defined in section 1297 without regard to subsection (d) thereof), and

(H) a REMIC.

(d) Constructive ownership transaction

For purposes of this section—

(1) In general

The taxpayer shall be treated as having entered into a constructive ownership transaction with respect to any financial asset if the taxpayer—

(A) holds a long position under a notional principal contract with respect to the financial asset,

(B) enters into a forward or futures contract to acquire the financial asset,

(C) is the holder of a call option, and is the grantor of a put option, with respect to the financial asset and such options have substantially equal strike prices and substantially contemporaneous maturity dates, or

(D) to the extent provided in regulations prescribed by the Secretary, enters into one or more other transactions (or acquires one or more positions) that have substantially the same effect as a transaction described in any of the preceding subparagraphs.

(2) Exception for positions which are marked to market

This section shall not apply to any constructive ownership transaction if all of the positions which are part of such transaction are marked to market under any provision of this title or the regulations thereunder.

(3) Long position under notional principal contract

A person shall be treated as holding a long position under a notional principal contract with respect to any financial asset if such person—

(A) has the right to be paid (or receive credit for) all or substantially all of the investment yield (including appreciation) on such financial asset for a specified period, and

(B) is obligated to reimburse (or provide credit for) all or substantially all of any decline in the value of such financial asset.