

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

Sec.	
451.	General rule for taxable year of inclusion.
[452.	Repealed.]
453.	Installment method.
453A.	Special rules for nondealers.
453B.	Gain or loss on disposition of installment obligations. <sup>1</sup>
[453C.	Repealed.]
454.	Obligations issued at discount.
455.	Prepaid subscription income.
456.	Prepaid dues income of certain membership organizations.
457.	Deferred compensation plans of State and local governments and tax-exempt organizations.
457A.	Nonqualified deferred compensation from certain tax indifferent parties.
458.	Magazines, paperbacks, and records returned after the close of the taxable year.
460.	Special rules for long-term contracts.

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

<sup>1</sup> So in original. Does not conform to section catchline.

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) 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.

(c) 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.

(d) 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.

**(e) 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.

**(f) 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.

**(g) 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).

**(h) 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).

**(i) 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, 2010, 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 con-

sists 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.)

REFERENCES IN TEXT

The Agricultural Act of 1949, as amended, referred to in subsec. (d), 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. (d), 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

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 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 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) of the Internal Revenue Code of 1986 (as added by such amendment)—

“(A) clause (ii) of such section 451(h)(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

Section 913(c) of Pub. L. 105-34 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.

Section 6030(b) of Pub. L. 100-647 provided that: “The amendment made by subsection (a) [amending this section] shall apply to sales or exchanges occurring after December 31, 1987.”

Section 6033(b) of Pub. L. 100-647, 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

Section 821(b) of Pub. L. 99-514, 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) 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.”

Section 905(c) of Pub. L. 99-514, 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) of the Internal Revenue Code of 1986 (as added by subsection (b)).”

#### EFFECTIVE DATE OF 1976 AMENDMENT

Section 2102(c) of Pub. L. 94-455 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.”

Section 2141(b) of Pub. L. 94-455 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

Section 215(b) of Pub. L. 91-172 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:

<b>“If the taxable year begins in calendar year:</b>	<b>The applicable percentage is:</b>
1983 .....	33⅓
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 (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 transactions 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 semi-annually.

##### (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 “(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

Section 10202(e) of Pub. L. 100-203, 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.

Section 812(c) of Pub. L. 99-514, 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:

<b>The applicable percentage is:</b>	
<b>“In the case of the:</b>	
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

Section 112(b) of Pub. L. 98-369 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

Section 311(a) of Pub. L. 97-448 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

Section 6(a) of Pub. L. 96-471, 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 453(b).—Section 453(b) 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 without 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) or 1201 (whichever is appropriate) 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.)

PRIOR PROVISIONS

Provisions similar to those comprising this section were contained in former section 453 of this title.

AMENDMENTS

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 subssecs. (a) to (d) provisions of former subssecs. (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 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.

Section 5076(c) of Pub. L. 100-647 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

Section 6031 of Pub. L. 100-647 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 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 dis-

position, 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 (as defined in section 806(b)(3)).

**(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.)

PRIOR PROVISIONS

Provisions similar to those comprising this section were contained in former section 453 of this title.

AMENDMENTS

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 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.

Section 1011(c)(1) of Pub. L. 99-514 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)

Section 217(b) of Pub. L. 98-369, 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 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**

Section 811(c) of Pub. L. 99-514, 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) 12½ 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-ex-

empt 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 method. 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

Section 28(c) of Pub. L. 85-866 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

Section 2 of Pub. L. 87-109 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,

(ii) when the participant has a severance from employment with the employer, or

(iii) when the participant is faced with an unforeseeable emergency (determined in the manner prescribed by the Secretary in regulations),

(B) the plan meets the minimum distribution requirements of paragraph (2), and

(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).

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 subpara-

graph (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 \$3,000.

**(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 9101 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 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 shall be the amount determined in accordance with the following table:

For taxable years beginning in calendar year:	The applicable dollar amount:
2002 .....	\$11,000
2003 .....	\$12,000
2004 .....	\$13,000
2005 .....	\$14,000
2006 or thereafter .....	\$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 9101 of the Elementary and Secondary Education Act of 1965 (20 U.S.C. 7801),<sup>1</sup> or

(ii) an education association which principally represents employees of 1 or more

<sup>1</sup> So in original. A second closing parenthesis probably should precede the comma.

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.)

**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.*

**AMENDMENTS**

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 “33½ 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 temporarily 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 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.

Section 1447(c) of Pub. L. 104-188 provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1996.”

Section 1448(c) of Pub. L. 104-188 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.”

Section 1458(c)(1) of Pub. L. 104-188 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

Section 1011(e)(9) of Pub. L. 100-647 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.

Section 6064(d) of Pub. L. 100-647 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

Section 1107(c) of Pub. L. 99-514, 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

Section 131(c)(1) of Pub. L. 95-600 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

Section 131(c)(2) of Pub. L. 95-600, 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) 33½ 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

Section 131(c)(3) of Pub. L. 95-600, 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 lim-

itations 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<sup>1</sup> a foreign corporation with income which is taxable under section 882, this

section shall not apply to compensation which, had such compensation had<sup>2</sup> 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.)

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

<sup>1</sup> So in original. Probably should be followed by “of”.

<sup>2</sup> So in original. The word “had” probably should not appear.

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) Repurchased<sup>1</sup> 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<sup>2</sup> 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

<sup>1</sup> So in original. Probably should be “Repurchase”.

<sup>2</sup> So in original. Probably should be “prescribe”.

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.)

EFFECTIVE DATE

Section 372(c) of Pub. L. 95-600 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<sup>1</sup> 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)

<sup>1</sup> So in original. Probably should be followed by a comma.

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 income 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 tax-

payer 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.

**(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—

(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) 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.

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) Determination of taxpayer’s gross receipts**

For purposes of paragraph (1), the gross receipts of—

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

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

(C) any predecessor of the taxpayer or a person described in subparagraph (A) or (B),

for the 3 taxable years of such persons preceding the taxable year in which the contract described in paragraph (1) is entered into shall be included in the gross receipts of the taxpayer for the period described in paragraph (1)(B). 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.

**(3) Controlled group of corporations**

For purposes of this subsection, the term “controlled group of corporations” has the meaning given to such term by section 1563(a), except that—

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

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

**(4) 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.

**(5) 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”.

**(6) 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.)

REFERENCES IN TEXT

The date of the enactment of the Revenue Reconciliation Act of 1989, referred to in subsec. (e)(5), is the date of enactment of title VII of Pub. L. 101-239, which was approved Dec. 19, 1989.

AMENDMENTS

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 1997 AMENDMENT

Section 1211(c) of Pub. L. 105-34 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

Section 7621(d) of Pub. L. 101-239 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 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.

Section 5041(e) of Pub. L. 100-647, 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

Section 10203(b) of Pub. L. 100-203 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

Section 804(d) of Pub. L. 99-514, 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

Section 804(b) of Pub. L. 99-514 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

Sec.

461. General rule for taxable year of deduction.