

periodical exists for such trade or business, but later wishes to make such election, it must apply for permission from the Commissioner. Such application shall be made in accordance with the provisions of section 446(e) and the regulations thereunder.

[T.D. 6591, 27 FR 1799, Feb. 27, 1962]

**§ 1.456-1 Treatment of prepaid dues income.**

Effective for taxable years beginning after December 31, 1960, a taxpayer which is a membership organization (as described in paragraph (c) of § 1.456-5) and which receives prepaid dues income as described in paragraph (a) of § 1.456-5 in connection with its trade or business of rendering services or making available membership privileges may elect under section 456 to include such income in gross income ratably over the taxable years during which its liability (as described in paragraph (b) of § 1.456-5) to render such services or extend such privileges exists, if such liability does not extend over a period of time in excess of 36 months. If the taxpayer does not elect to treat prepaid dues income under section 456, or if such income may not be reported under section 456, as for example, where the income relates to a liability to render services or make available membership privileges which extends beyond 36 months, then such income is includible in gross income for the taxable year in which it is received (as described in paragraph (d) of § 1.456-5).

[T.D. 6937, 32 FR 16394, Nov. 30, 1967]

**§ 1.456-2 Scope of election under section 456.**

(a) An election made under section 456 and § 1.456-6, shall be applicable to all prepaid dues income received in connection with the trade or business for which the election is made. However, the taxpayer may further elect to include in gross income for the taxable year of receipt the entire amount of any prepaid dues income attributable to a liability extending beyond the close of the taxable year but ending within 12 months after the date of receipt, hereinafter referred to as the "within 12 months" election.

(b) If the taxpayer is engaged in more than one trade or business in connection with which prepaid dues income is received, a separate election may be made under section 456 with respect to each such trade or business. In addition, a taxpayer may make a separate "within 12 months" election for each separate trade or business for which it has made an election under section 456.

(c) A section 456 election and a "within 12 months" election shall be binding for the first taxable year for which the election is made and for all subsequent taxable years, unless the taxpayer secures the consent of the Commissioner to the revocation of either election. In order to secure the Commissioner's consent to the revocation of the section 456 election or the "within 12 months" election, an application must be filed with the Commissioner in accordance with section 446(e) and the regulations thereunder. However, an application for consent to revoke the section 456 election or the "within 12 months" election in the case of all taxable years which end before November 30, 1967 must be filed on or before February 28, 1968. For purposes of Subtitle A of the Code, the computation of taxable income under an election made under section 456 or under the "within 12 months" election shall be treated as a method of accounting. For adjustments required by changes in method of accounting, see section 481 and the regulations thereunder.

(d) Except as provided in section 456(d) and § 1.456-7, an election made under section 456 shall not apply to any prepaid dues income received before the first taxable year to which the election applies. For example, Corporation X, a membership organization which files its income tax returns on a calendar year basis, customarily sells 3-year memberships, payable in advance. In 1961 it received \$160,000 of prepaid dues income for 3-year memberships beginning during 1961, and in 1962 it received \$185,000 of prepaid dues income for 3-year memberships beginning on January 1, 1962. In March 1962 it elected, with the consent of the Commissioner, to report its prepaid dues income under the provisions of section 456 for the year 1962 and subsequent

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taxable years. The \$160,000 received in 1961 from prepaid dues must be included in gross income in full in that year, and except as provided in section 456(d) and § 1.456-7, no part of such income shall be allocated to the taxable years 1962, 1963, and 1964 during which X was under a liability to make available its membership privileges. The \$185,000 received in 1962 from prepaid dues income shall be allocated to the years 1962, 1963, and 1964.

(e) No election may be made under section 456 with respect to a trade or business if, in computing taxable income, the cash receipts and disbursements method (or a hybrid thereof) of accounting is used with respect to such trade or business, unless the combination of the section 456 election and the taxpayer's hybrid method of accounting does not result in a material distortion of income.

[T.D. 6937, 32 FR 16394, Nov. 30, 1967; 32 FR 17479, Dec. 6, 1967]

#### § 1.456-3 Method of allocation.

(a) Prepaid dues income for which an election has been made under section 456 shall be included in gross income over the period of time during which the liability to render services or make available membership privileges exists. The liability to render the services or make available the membership privileges shall be deemed to exist ratably over the period of time such services are required to be rendered, or such membership privileges are required to be made available. Thus, the prepaid dues income shall be included in gross income ratably over the period of the membership contract. For example, Corporation X, a membership organization, which files its income tax returns on a calendar year basis, elects, for its taxable year beginning January 1, 1961, to report its prepaid dues income in accordance with the provisions of section 456. On March 31, 1961, it sells a 2-year membership for \$48 payable in advance, the membership to extend from May 1, 1961, to April 30, 1963. X shall include in its gross income for the taxable year 1961  $\frac{3}{24}$  of the \$48, or \$16, and for the taxable year 1962  $\frac{12}{24}$  of the \$48, or \$24, and for the taxable year 1963  $\frac{4}{24}$  of the \$48, or \$8.

(b) For purposes of determining the period or periods over which the liability of the taxpayer exists, and for purposes of allocating prepaid dues income to such periods, the taxpayer may aggregate similar transactions during the taxable year in any reasonable manner, provided the method of aggregation and allocation is consistently followed.

[T.D. 6937, 32 FR 16395, Nov. 30, 1967]

#### § 1.456-4 Cessation of liability or existence.

(a) If a taxpayer has elected to apply the provisions of section 456 to a trade or business in connection with which prepaid dues income is received, and if the taxpayer's liability to render services or make available membership privileges ends for any reason, as for example, because of the cancellation of a membership then so much of the prepaid dues income attributable to such liability as was not includible in the taxpayer's gross income under section 456 for preceding taxable years shall be included in gross income for the taxable year in which such liability ends. This paragraph shall not apply to amounts includible in gross income under § 1.456-7.

(b) If a taxpayer which has elected to apply the provisions of section 456 ceases to exist, then the prepaid dues income which was not includible in gross income under section 456 for preceding taxable years shall be included in the taxpayer's gross income for the taxable year in which such cessation of existence occurs. This paragraph shall not apply to amounts includible in gross income under § 1.456-7.

(c) If a taxpayer is a party to a transaction to which section 381(a) applies and the taxpayer's method of accounting with respect to prepaid dues income is used by the acquiring corporation under the provisions of section 381(c)(4), then neither the liability nor the existence of the taxpayer shall be deemed to have ended or ceased. In such cases see section 381(c)(4) and the regulations thereunder for the treatment of the portion of prepaid dues income which was not included in gross income under section 456 for preceding taxable years.

[T.D. 6937, 32 FR 16395, Nov. 30, 1967]