

being taken less frequently than annually. In addition, the Commissioner may prescribe procedures indicating that samples made to update the results of a sample of stamps redeemed in a prior year need not be the same size as the sample of such prior year.

(d) *Consistency with financial reporting*—(1) *Estimated future redemptions.* For taxable years beginning after August 22, 1972, the estimated future redemptions must be no greater than the estimate that the taxpayer uses for purposes of all reports (including consolidated financial statements) to shareholders, partners, beneficiaries, other proprietors, and for credit purposes.

(2) *Average cost of redeeming stamps.* For taxable years beginning after August 22, 1972, the estimated average cost of redeeming each stamp or coupon must be no greater than the average cost of redeeming each stamp or coupon (computed in accordance with paragraph (b)(1)(iii) of this section) that the taxpayer uses for purposes of all reports (including consolidated financial statements) to shareholders, partners, beneficiaries, other proprietors, and for credit purposes.

(e) *Information to be furnished with return*—(1) *In general.* For taxable years beginning after August 22, 1972, a taxpayer described in paragraph (a) of this section who uses a method of determining the “estimated future redemptions” other than that described in paragraph (c)(5)(i) of this section shall file a statement with his return showing such information as is necessary to establish the correctness of the amount subtracted from gross receipts in the taxable year.

(2) *Taxpayers using the 5-year rule.* If a taxpayer uses the method of determining estimated future redemptions described in paragraph (c)(5)(i) of this section, he shall file a statement with his return showing, with respect to the taxable year and the 4 preceding taxable years—

(i) The total number of stamps or coupons issued or sold during each year, and

(ii) The total number of stamps or coupons redeemed in each such year.

(3) *Trading stamp companies.* In addition to the information required by

subparagraph (1) or (2) of this paragraph, a taxpayer engaged in the trade or business of selling trading stamps or premium coupons shall include with the statement described in subparagraph (1) or (2) of this paragraph such information as may be necessary to satisfy the requirements of paragraph (a)(2)(iv) of this section.

[T.D. 7201, 37 FR 16911, Aug. 23, 1972, as amended by T.D. 7201, 37 FR 18617, Sept. 14, 1972]

**§ 1.451-5 Advance payments for goods and long-term contracts.**

(a) *Advance payment defined.* (1) For purposes of this section, the term “advance payment” means any amount which is received in a taxable year by a taxpayer using an accrual method of accounting for purchases and sales or a long-term contract method of accounting (described in § 1.451-3), pursuant to, and to be applied against, an agreement:

(i) For the sale or other disposition in a future taxable year of goods held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or

(ii) For the building, installing, constructing or manufacturing by the taxpayer of items where the agreement is not completed within such taxable year.

(2) For purposes of subparagraph (1) of this paragraph:

(i) The term “agreement” includes (a) a gift certificate that can be redeemed for goods, and (b) an agreement which obligates a taxpayer to perform activities described in subparagraph (1)(i) or (ii) of this paragraph and which also contains an obligation to perform services that are to be performed as an integral part of such activities; and

(ii) Amounts due and payable are considered “received”.

(3) If a taxpayer (described in subparagraph (1) of this paragraph) receives an amount pursuant to, and to be applied against, an agreement that not only obligates the taxpayer to perform the activities described in subparagraph (1) (i) and (ii) of this paragraph, but also obligates the taxpayer to perform services that are not to be performed as an integral part of such activities, such amount will be treated

as an “advance payment” (as defined in subparagraph (1) of this paragraph) only to the extent such amount is properly allocable to the obligation to perform the activities described in subparagraph (1) (i) and (ii) of this paragraph. The portion of the amount not so allocable will not be considered an “advance payment” to which this section applies. If, however, the amount not so allocable is less than 5 percent of the total contract price, such amount will be treated as so allocable except that such treatment cannot result in delaying the time at which the taxpayer would otherwise accrue the amounts attributable to the activities described in subparagraph (1) (i) and (ii) of this paragraph.

(b) *Taxable year of inclusion*—(1) *In general.* Advance payments must be included in income either—

- (i) In the taxable year of receipt; or
- (ii) Except as provided in paragraph (c) of this section.

(a) In the taxable year in which properly accruable under the taxpayer’s method of accounting for tax purposes if such method results in including advance payments in gross receipts no later than the time such advance payments are included in gross receipts for purposes of all of his reports (including consolidated financial statements) to shareholders, partners, beneficiaries, other proprietors, and for credit purposes, or

(b) If the taxpayer’s method of accounting for purposes of such reports results in advance payments (or any portion of such payments) being included in gross receipts earlier than for tax purposes, in the taxable year in which includible in gross receipts pursuant to his method of accounting for purposes of such reports.

(2) *Examples.* This paragraph may be illustrated by the following examples:

*Example (1).* S, a retailer who uses for tax purposes and for purposes of the reports referred to in subparagraph (1)(ii)(a) of this paragraph, an accrual method of accounting under which it accounts for its sales of goods when the goods are shipped, receives advance payments for such goods. Such advance payments must be included in gross receipts for tax purposes either in the taxable year the payments are received or in the taxable year such goods are shipped (except as provided in paragraph (c) of this section).

*Example (2).* T, a manufacturer of household furniture, is a calendar year taxpayer who uses an accrual method of accounting pursuant to which income is accrued when furniture is shipped for purposes of its financial reports (referred to in subparagraph (1)(ii)(a) of this paragraph) and an accrual method of accounting pursuant to which the income is accrued when furniture is delivered and accepted for tax purposes. See § 1.446-1(c)(1)(ii). In 1974, T receives an advance payment of \$8,000 from X with respect to an order of furniture to be manufactured for X for a total price of \$20,000. The furniture is shipped to X in December 1974, but it is not delivered to and accepted by X until January 1975. As a result of this contract, T must include the entire advance payment in its gross income for tax purposes in 1974 pursuant to subparagraph (1)(ii)(b) of this paragraph. T must include the remaining \$12,000 of the gross contract price in its gross income in 1975 for tax purposes.

(3) *Long-term contracts.* In the case of a taxpayer accounting for advance payments for tax purposes pursuant to a long-term contract method of accounting under § 1.460-4, or of a taxpayer accounting for advance payments with respect to a long-term contract pursuant to an accrual method of accounting referred to in the succeeding sentence, advance payments shall be included in income in the taxable year in which properly included in gross receipts pursuant to such method of accounting (without regard to the financial reporting requirement contained in subparagraph (1)(ii) (a) or (b) of this paragraph). An accrual method of accounting to which the preceding sentence applies shall consist of any method of accounting under which the income is accrued when, and costs are accumulated until, the subject matter of the contract (or, if the subject matter of the contract consists of more than one item, an item) is shipped, delivered, or accepted.

(4) *Installment method.* The financial reporting requirement of subparagraph (1)(ii) (a) or (b) of this paragraph shall not be construed to prevent the use of the installment method under section 453. See § 1.446-1(c)(1)(ii).

(c) *Exception for inventoriable goods.* (1)(i) If a taxpayer receives an advance payment in a taxable year with respect to an agreement for the sale of goods properly includible in his inventory, or with respect to an agreement (such as

a gift certificate) which can be satisfied with goods or a type of goods that cannot be identified in such taxable year, and on the last day of such taxable year the taxpayer—

(a) Is accounting for advance payments pursuant to a method described in paragraph (b)(1)(ii) of this section for tax purposes,

(b) Has received “substantial advance payments” (as defined in subparagraph (3) of this paragraph) with respect to such agreement, and

(c) Has on hand (or available to him in such year through his normal source of supply) goods of substantially similar kind and in sufficient quantity to satisfy the agreement in such year,

then all advance payments received with respect to such agreement by the last day of the second taxable year following the year in which such substantial advance payments are received, and not previously included in income in accordance with the taxpayer’s accrual method of accounting, must be included in income in such second taxable year.

(ii) If advance payments are required to be included in income in a taxable year solely by reason of subdivision (i) of this subparagraph, the taxpayer must take into account in such taxable year the costs and expenditures included in inventory at the end of such year with respect to such goods (or substantially similar goods) on hand or, if no such goods are on hand by the last day of such second taxable year, the estimated cost of goods necessary to satisfy the agreement.

(iii) Subdivision (ii) of this subparagraph does not apply if the goods or type of goods with respect to which the advance payment is received are not identifiable in the year the advance payments are required to be included in income by reason of subdivision (i) of this subparagraph (for example, where an amount is received for a gift certificate).

(2) If subparagraph (1)(i) of this paragraph is applicable to advance payments received with respect to an agreement, any advance payments received with respect to such agreement subsequent to such second taxable year must be included in gross income in the taxable year of receipt. To the ex-

tent estimated costs of goods are taken into account in a taxable year pursuant to subparagraph (1)(ii) of this paragraph, such costs may not again be taken into account in another year. In addition, any variances between the costs or estimated costs taken into account pursuant to subparagraph (1)(ii) of this paragraph and the costs actually incurred in fulfilling the taxpayer’s obligations under the agreement must be taken into account as an adjustment to the cost of goods sold in the year the taxpayer completes his obligations under such agreement.

(3) For purposes of subparagraph (1) of this paragraph, a taxpayer will be considered to have received “substantial advance payments” with respect to an agreement by the last day of a taxable year if the advance payments received with respect to such agreement during such taxable year plus the advance payments received prior to such taxable year pursuant to such agreement, equal or exceed the total costs and expenditures reasonably estimated as includible in inventory with respect to such agreement. Advance payments received in a taxable year with respect to an agreement (such as a gift certificate) under which the goods or type of goods to be sold are not identifiable in such year shall be treated as “substantial advance payments” when received.

(4) The application of this paragraph is illustrated by the following example:

*Example.* In 1971, X, a calendar year accrual method taxpayer, enters into a contract for the sale of goods (properly includible in X’s inventory) with a total contract price of \$100. X estimates that his total inventoriable costs and expenditures for the goods will be \$50. X receives the following advance payments with respect to the contract:

1971 .....	\$35
1972 .....	20
1973 .....	15
1974 .....	10
1975 .....	10
1976 .....	10

The goods are delivered pursuant to the customer’s request in 1977. X’s closing inventory for 1972 of the type of goods involved in the contract is sufficient to satisfy the contract. Since advance payments received by the end of 1972 exceed the inventoriable costs X estimates that he will incur, such payments constitute “substantial advance payments”. Accordingly, all payments received by the end of 1974, the end of the second taxable year following the taxable year during

which “substantial advance payments” are received, are includible in gross income for 1974. Therefore, for taxable year 1974 X must include \$80 in his gross income. X must include in his cost of goods sold for 1974 the cost of such goods (or similar goods) on hand or, if no such goods are on hand, the estimated inventoriable costs necessary to satisfy the contract. Since no further deferral is allowable for such contract, X must include in his gross income for the remaining years of the contract, the advance payment received each year. Any variance between estimated costs and the costs actually incurred in fulfilling the contract is to be taken into account in 1977, when the goods are delivered. See paragraph (c)(2) of this section.

(d) *Information schedule.* If a taxpayer accounts for advance payments pursuant to paragraph (b)(1)(ii) of this section, he must attach to his income tax return for each taxable year to which such provision applies an annual information schedule reflecting the total amount of advance payments received in the taxable year, the total amount of advance payments received in prior taxable years which has not been included in gross income before the current taxable year, and the total amount of such payments received in prior taxable years which has been included in gross income for the current taxable year.

(e) *Adoption of method.* (1) For taxable years ending on or after December 31, 1969, and before January 1, 1971, a taxpayer (even if he has already filed an income tax return for a taxable year ending within such period) may secure the consent of the Commissioner to change his method of accounting for such year to a method prescribed in paragraph (b)(1)(ii) of this section in the manner prescribed in section 446 and the regulations thereunder, if an application to secure such consent is filed on Form 3115 within 180 days after March 23, 1971.

(2) A taxpayer who is already reporting his income in accordance with a method prescribed in paragraph (b)(1)(ii)(a) of this section need not secure the consent of the Commissioner to continue to utilize this method. However, such a taxpayer, for all taxable years ending after March 23, 1971, must comply with the requirements of paragraphs (b)(1)(ii)(a) (including the financial reporting requirement) and

(d) (relating to an annual information schedule) of this section.

(f) *Cessation of taxpayer’s liability.* If a taxpayer has adopted a method prescribed in paragraph (b)(1)(ii) of this section, and if in a taxable year the taxpayer dies, ceases to exist in a transaction other than one to which section 381(a) applies, or his liability under the agreement otherwise ends, then so much of the advance payment as was not includible in his gross income in preceding taxable years shall be included in his gross income for such taxable year.

(g) *Special rule for certain transactions concerning natural resources.* A transaction which is treated as creating a mortgage loan pursuant to section 636 and the regulations thereunder rather than as a sale shall not be considered a “sale or other disposition” within the meaning of paragraph (a)(1) of this section. Consequently, any payment received pursuant to such a transaction, which payment would otherwise qualify as an “advance payment”, will not be treated as an “advance payment” for purposes of this section.

[T.D. 7103, 36 FR 5495, Mar. 24, 1971, as amended by T.D. 7397, 41 FR 2641, Jan. 19, 1976; T.D. 8067, 51 FR 393, Jan. 6, 1986; T.D. 8929, 66 FR 2224, Jan. 11, 2001]

**§ 1.451-6 Election to include crop insurance proceeds in gross income in the taxable year following the taxable year of destruction or damage.**

(a) *In general.* (1) For taxable years ending after December 30, 1969, a taxpayer reporting gross income on the cash receipts and disbursements method of accounting may elect to include insurance proceeds received as a result of the destruction of, or damage to, crops in gross income for the taxable year following the taxable year of the destruction or damage, if the taxpayer establishes that, under the taxpayer’s normal business practice, the income from those crops would have been included in gross income for any taxable year following the taxable year of the destruction or damage. However, if the taxpayer receives the insurance proceeds in the taxable year following the