

dealer treats a sale on the installment plan as a transaction other than a sale and fails to report the full amount of gain in the year of the sale. For example, if a transaction treated by a dealer as a lease is recharacterized by the Internal Revenue Service as a sale on the installment plan, the dealer will be deemed to have elected the installment method assuming the dealer failed to report the full amount of gain in the year of the transaction.

(c) *Consent.* A dealer may adopt or change to the installment method for sales on the installment plan without the consent of the Commissioner. However, a dealer may not change from the installment method to the accrual method of accounting or to any other method of accounting without the consent of the Commissioner.

(d) *Cut-off method for amounts previously accrued.* An election to change to the installment method for a type of sale applies only with respect to sales made on or after the first day of the taxable year of change. Thus, payments received in the taxable year of the change, or in subsequent years, in respect of an installment obligation which arose in a taxable year prior to the taxable year of change are not taken into account on the installment method, but rather must be accounted for under the taxpayer's method of accounting in use in the prior year.

(e) *Effective date.* This section applies to sales by dealers in taxable years ending after October 19, 1980, but generally does not apply to sales made after December 31, 1987. For sales made after December 31, 1987, sales by a dealer in personal or real property shall not be treated as sales on the installment plan. (However, see section 453(l)(2) for certain exceptions to this rule.) For rules relating to sales by dealers in taxable years ending before October 20, 1980, see 26 CFR 1.453-7 and 1.453-8 (rev. as of April 1, 1987).

[T.D. 8269, 54 FR 46375, Nov. 3, 1989]

§ 1.454-1 Obligations issued at discount.

(a) *Certain non-interest-bearing obligations issued at discount—(1) Election to include increase in income currently.* If a taxpayer owns—

(i) A non-interest-bearing obligation issued at a discount and redeemable for fixed amounts increasing at stated intervals (other than an obligation issued by a corporation after May 27, 1969, as to which ratable inclusion of original issue discount is required under section 1232(a)(3)), or

(ii) An obligation of the United States, other than a current income obligation, in which he retains his investment in a matured series E U.S. savings bond, or

(iii) A nontransferable obligation (whether or not a current income obligation) of the United States for which a series E U.S. savings bond was exchanged (whether or not at final maturity) in an exchange upon which gain is not recognized because of section 1037(a) (or so much of section 1031(b) as relates to section 1037),

and if the increase, if any, in redemption price of such obligation described in subdivision (i), (ii), or (iii) of this subparagraph during the taxable year (as described in subparagraph (2) of this paragraph) does not constitute income for such year under the method of accounting used in computing his taxable income, then the taxpayer may, at his election, treat the increase as constituting income for the year in which such increase occurs. If the election is not made and section 1037 (or so much of section 1031 as relates to section 1037) does not apply, the taxpayer shall treat the increase as constituting income for the year in which the obligation is redeemed or disposed of, or finally matures, whichever is earlier. Any such election must be made in the taxpayer's return and may be made for any taxable year. If an election is made with respect to any such obligation described in subdivision (i), (ii), or (iii) of this subparagraph, it shall apply also to all other obligations of the type described in such subdivisions owned by the taxpayer at the beginning of the first taxable year to which the election applies, and to those thereafter acquired by him, and shall be binding for the taxable year for which the return is filed and for all subsequent taxable years, unless the Commissioner permits the taxpayer to change to a different method of reporting income from such obligations. See section

446(e) and paragraph (e) of §1.446-1, relating to requirement respecting a change of accounting method. Although the election once made is binding upon the taxpayer, it does not apply to a transferee of the taxpayer.

(2) *Amount of increase in case of non-interest-bearing obligations.* In any case in which an election is made under section 454, the amount which accrues in any taxable year to which the election applies is measured by the actual increase in the redemption price occurring in that year. This amount does not accrue ratably between the dates on which the redemption price changes. For example, if two dates on which the redemption price increases (February 1 and August 1) fall within a taxable year and if the redemption price increases in the amount of 50 cents on each such date, the amount accruing in that year would be \$1 (\$0.50 on February 1 and \$0.50 on August 1). If the taxpayer owns a non-interest-bearing obligation of the character described in subdivision (i), (ii), or (iii) of subparagraph (1) of this paragraph acquired prior to the first taxable year to which his election applies, he must also include in gross income for such first taxable year (i) the increase in the redemption price of such obligation occurring between the date of acquisition of the obligation and the first day of such first taxable year and (ii), in a case where a series E bond was exchanged for such obligation, the increase in the redemption price of such series E bond occurring between the date of acquisition of such series E bond and the date of the exchange.

(3) *Amount of increase in case of current income obligations.* If an election is made under section 454 and the taxpayer owns, at the beginning of the first taxable year to which the election applies, a current income obligation of the character described in subparagraph (1)(iii) of this paragraph acquired prior to such taxable year, he must also include in gross income for such first taxable year the increase in the redemption price of the series E bond which was surrendered to the United States in exchange for such current income obligation; the amount of the increase is that occurring between the

date of acquisition of the series E bond and the date of the exchange.

(4) *Illustrations.* The application of this paragraph may be illustrated by the following examples:

Example (1). Throughout the calendar year 1954, a taxpayer who uses the cash receipts and disbursements method of accounting holds series E U.S. savings bonds having a maturity value of \$5,000 and a redemption value at the beginning of the year 1954 of \$4,050 and at the end of the year 1954 of \$4,150. He purchased the bonds on January 1, 1949, for \$3,750, and holds no other obligation of the type described in this section. If the taxpayer exercises the election in his return for the calendar year 1954, he is required to include \$400 in taxable income with respect to such bonds. Of this amount, \$300 represents the increase in the redemption price before 1954 and \$100 represents the increase in the redemption price in 1954. The increases in redemption value occurring in subsequent taxable years are includible in gross income for such taxable years.

Example (2). In 1958 B, a taxpayer who uses the cash receipts and disbursements method of accounting and the calendar year as his taxable year, purchased for \$7,500 a series E United States savings bond with a face value of \$10,000. In 1965, when the stated redemption value of the series E bond is \$9,760, B surrenders it to the United States in exchange solely for a \$10,000 series H U.S. current income savings bond in an exchange qualifying under section 1037(a), after paying \$240 additional consideration. On the exchange of the series E bond for the series H bond in 1965, B realizes a gain of \$2,260 (\$9,760 less \$7,500), none of which is recognized for that year by reason of section 1037(a). B retains the series H bond and redeems it at maturity in 1975 for \$10,000, but in 1966 he exercises the election under section 454(a) in his return for that year with respect to five series E bonds he purchased in 1960. B is required to include in gross income for 1966 the increase in redemption price occurring before 1966 and in 1966 with respect to the series E bonds purchased in 1960; he is also required to include in gross income for 1966 the \$2,260 increase in redemption price of the series E bond which was exchanged in 1965 for the series H bond.

(b) *Short-term obligations issued on a discount basis.* In the case of obligations of the United States or any of its possessions, or of a State, or Territory, or any political subdivision thereof, or of the District of Columbia, issued on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, the amount of discount at which such

obligation originally sold does not accrue until the date on which such obligation is redeemed, sold, or otherwise disposed of. This rule applies regardless of the method of accounting used by the taxpayer. For examples illustrating rules for computation of income from sale or other disposition of certain obligations of the type described in this paragraph, see section 1221 and the regulations thereunder.

(c) *Matured U.S. savings bonds*—(1) *Inclusion of increase in income upon redemption or final maturity.* If a taxpayer (other than a corporation) holds—

(i) A matured series E U.S. savings bond,

(ii) An obligation of the United States, other than a current income obligation, in which he retains his investment in a matured series E U.S. savings bond, or

(iii) A nontransferable obligation (whether or not a current income obligation) of the United States for which a series E U.S. savings bond was exchanged (whether or not at final maturity) in an exchange upon which gain is not recognized because of section 1037(a) (or so much of section 1031(b) as relates to section 1037(a)),

the increase in redemption price of the series E bond in excess of the amount paid for such series E bond shall be included in the gross income of such taxpayer for the taxable year in which the obligation described in subdivision (i), (ii), or (iii) of this subparagraph is redeemed or disposed of, or finally matures, whichever is earlier, but only to the extent such increase has not previously been includible in the gross income of such taxpayer or any other taxpayer. If such obligation is partially redeemed before final maturity, or partially disposed of by being partially reissued to another owner, such increase in redemption price shall be included in the gross income of such taxpayer for such taxable year on a basis proportional to the total denomination of obligations redeemed or disposed of. The provisions of section 454 (c) and of this subparagraph 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 a taxable year for which an election made by the taxpayer under sec-

tion 454(a) and paragraph (a) of this section applies. For rules respecting the character of the gain realized upon the disposition or redemption of an obligation described in subdivision (iii) of this subparagraph, see paragraph (b) of § 1.1037-1.

(2) *Illustrations.* The application of this paragraph may be illustrated by the following examples, in which it is assumed that the taxpayer uses the cash receipts and disbursements method of accounting and the calendar year as his taxable year:

Example (1). On June 1, 1941, A purchased for \$375 a series E U.S. savings bond which was redeemable at maturity (10 years from issue date) for \$500. At maturity of the bond, A exercised the option of retaining the matured series E bond for the 10-year extended maturity period. On June 2, 1961, A redeemed the series E bond, at which time the stated redemption value was \$674.60. A never elected under section 454(a) to include the annual increase in redemption price in gross income currently. Under section 454(c), A is required to include \$299.60 (\$674.60 less \$375) in gross income for 1961 by reason of his redemption of the bond.

Example (2). The facts are the same as in example (2) in paragraph (a)(4) of this section. On redemption of the series H bond received in the exchange qualifying under section 1037(a), B realizes a gain of \$2,260, determined as provided in example (5) in paragraph (b)(4) of § 1.1037-1. None of this amount is includible in B's gross income for 1975, such amount having already been includible in his gross income for 1966 because of his election under section 454(a).

Example (3). C, who had elected under section 454(a) to include the annual increase in the redemption price of his non-interest-bearing obligations in gross income currently, owned a \$1,000 series E U.S. savings bond, which was purchased on October 1, 1949, for \$750, C died on February 1, 1955, when the redemption value of the bond was \$820. The bond was immediately reissued to D, his only heir, who has not made an election under section 454(a). On January 15, 1960, when the redemption value of the bond is \$1,000, D surrenders it to the United States in exchange solely for a \$1,000 series H U.S. savings bond in an exchange qualifying under the provisions of section 1037(a). For 1960 D properly does not return any income from the exchange of bonds, although he returns the interest payments on the series H bond for the taxable years in which they are received. On September 1, 1964, prior to maturity of the series H bond, D redeems it for \$1,000. For 1964, D must include \$180 in gross

income under section 454(c) from the redemption of the series H bond, that is, the amount of the increase in the redemption price of the series E bond (\$1,000 less \$820) occurring between February 1, 1955, and January 15, 1960, the period during which he owned the series E bond.

[T.D. 6500, 25 FR 11719, Nov. 26, 1960, as amended by T.D. 6935, 32 FR 15820, Nov. 17, 1967; T.D. 7154, 36 FR 24997, Dec. 28, 1971]

§ 1.455-1 Treatment of prepaid subscription income.

Effective with respect to taxable years beginning after December 31, 1957, section 455 permits certain taxpayers to elect with respect to a trade or business in connection with which prepaid subscription income is received, to include such income in gross income for the taxable years during which a liability exists to furnish or deliver a newspaper, magazine, or other periodical. If a taxpayer does not elect to treat prepaid subscription income under the provisions of section 455, such income is includible in gross income for the taxable year in which received by the taxpayer, unless under the method or practice of accounting used in computing taxable income such amount is to be properly accounted for as of a different period.

[T.D. 6591, 27 FR 1798, Feb. 27, 1962]

§ 1.455-2 Scope of election under section 455.

(a) If a taxpayer makes an election under section 455 and § 1.455-6 with respect to a trade or business, all prepaid subscription income from such trade or business shall be included in gross income for the taxable years during which the liability exists to furnish or deliver a newspaper, magazine, or other periodical. Such election shall be applicable to all prepaid subscription income received in connection with the trade or business for which the election is made; except that the taxpayer may further elect to include in gross income for the taxable year of receipt (as described in section 455(d)(3) and paragraph (c) of § 1.455-5) 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, hereinafter sometimes referred to as “within 12 months” election.

(b) If the taxpayer is engaged in more than one trade or business in which a liability is incurred to furnish or deliver a newspaper, magazine, or other periodical, a separate election 455 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 455.

(c) An election made under section 455 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 such election. Thus, in any case where the taxpayer has elected a method prescribed by section 455 for the inclusion of prepaid subscription income in gross income, such method of reporting income may not be changed without the prior approval of the Commissioner. In order to secure the Commissioner’s consent to the revocation of such election, an application must be filed with the Commissioner in accordance with section 446(e) and the regulations thereunder. For purposes of subtitle A of the Code, the computation of taxable income under an election made under section 455 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) An election made under section 455 shall not apply to any prepaid subscription income received before the first taxable year to which the election applies. For example, Corporation M, which computes its taxable income under an accrual method of accounting and files its income tax returns on the calendar year basis, publishes a monthly magazine and customarily sells subscriptions on a 3-year basis. In 1958 it received \$135,000 of 3-year prepaid subscription income for subscriptions beginning during 1958, and in 1959 it received \$142,000 of prepaid subscription income for subscriptions beginning after December 31, 1958. In February 1959 it elected, with the consent of the Commissioner, to report its prepaid subscription income under the provisions of section 455 for the year 1959 and subsequent taxable years. The