

indication that the election is being made under paragraph (b)(2)(i) of this section. Both the buyer and the seller must sign this statement not later than the earlier of the last day (including extensions) for filing the Federal income tax return of the buyer or seller for the taxable year in which the sale or exchange of the property occurs. The buyer and seller should attach this signed statement (or a copy thereof) to their timely filed Federal income tax returns.

(c) *Wraparound indebtedness.* For purposes of paragraph (a) of this section, the issuance of wraparound indebtedness is not considered an assumption.

(d) *Consideration attributable to assumed debt.* If, as part of the consideration for the sale or exchange of property, the buyer assumes, or takes the property subject to, an indebtedness that was issued with OID (including a debt instrument issued in a prior sale or exchange to which section 1274 applied), the portion of the buyer's basis in the property and the seller's amount realized attributable to the debt instrument equals the adjusted issue price of the debt instrument as of the date of the sale or exchange.

[T.D. 8517, 59 FR 4824, Feb. 2, 1994]

§ 1.1274A-1 Special rules for certain transactions where stated principal amount does not exceed \$2,800,000.

(a) *In general.* Section 1274A allows the use of a lower test rate for purposes of sections 483 and 1274 in the case of a qualified debt instrument (as defined in section 1274A(b)) and, if elected by the borrower and the lender, the use of the cash receipts and disbursements method of accounting for interest on a cash method debt instrument (as defined in section 1274A(c)(2)). This section provides special rules for qualified debt instruments and cash method debt instruments.

(b) *Rules for both qualified and cash method debt instruments—(1) Sale-leaseback transactions.* A debt instrument issued in a sale-leaseback transaction (within the meaning of section 1274(e)) cannot be either a qualified debt instrument or a cash method debt instrument.

(2) *Debt instruments calling for contingent payments.* A debt instrument that

provides for contingent payments cannot be a qualified debt instrument unless it can be determined at the time of the sale or exchange that the maximum stated principal amount due under the debt instrument cannot exceed the amount specified in section 1274A(b). Similarly, a debt instrument that provides for contingent payments cannot be a cash method debt instrument unless it can be determined at the time of the sale or exchange that the maximum stated principal amount due under the debt instrument cannot exceed the amount specified in section 1274A(c)(2)(A).

(3) *Aggregation of transactions—(i) General rule.* The aggregation rules of section 1274A(d)(1) are applied using a facts and circumstances test.

(ii) *Examples.* The following examples illustrate the application of section 1274A(d)(1) and paragraph (b)(3)(i) of this section.

Example 1. Aggregation of two sales to a single person. In two transactions evidenced by separate sales agreements, A sells undivided half interests in Blackacre to B. The sales are pursuant to a plan for the sale of a 100 percent interest in Blackacre to B. These sales or exchanges are part of a series of related transactions and, thus, are treated as a single sale for purposes of section 1274A.

Example 2. Aggregation of two purchases by unrelated individuals. Pursuant to a plan, unrelated individuals X and Y purchase undivided half interests in Blackacre from A and subsequently contribute these interests to a partnership in exchange for equal interests in the partnership. These purchases are treated as part of the same transaction and, thus, are treated as a single sale for purposes of section 1274A.

Example 3. Aggregation of sales made pursuant to a tender offer. Fifteen unrelated individuals own all of the stock of X Corporation. Y Corporation makes a tender offer to these 15 shareholders. The terms offered to each shareholder are identical. Shareholders holding a majority of the shares of X Corporation elect to tender their shares pursuant to Y Corporation's offer. These sales are part of the same transaction and, thus, are treated as a single sale for purposes of section 1274A.

Example 4. No aggregation for separate sales of similar property to unrelated persons. Pursuant to a newspaper advertisement, X Corporation offers for sale similar condominiums in a single building. The prices of the units vary due to a variety of factors, but the financing terms offered by X Corporation

to all buyers are identical. The units are purchased by unrelated buyers who decided whether to purchase units in the building at the price and on the terms offered by X Corporation, without regard to the actions of other buyers. Because each buyer acts individually, the sales are not part of the same transaction or a series of related transactions and, thus, are treated as separate sales.

(4) *Inflation adjustment of dollar amounts.* Under section 1274A(d)(2), the dollar amounts specified in sections 1274A(b) and 1274A(c)(2)(A) are adjusted for inflation. The dollar amounts, adjusted for inflation, are published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii) of this chapter).

(c) *Rules for cash method debt instruments—(1) Time and manner of making cash method election.* The borrower and lender make the election described in section 1274A(c)(2)(D) by jointly signing a statement that includes the names, addresses, and taxpayer identification numbers of the borrower and lender, a clear indication that an election is being made under section 1274A(c)(2), and a declaration that the debt instrument with respect to which the election is being made fulfills the requirements of a cash method debt instrument. Both the borrower and the lender must sign this statement not later than the earlier of the last day (including extensions) for filing the Federal income tax return of the borrower or lender for the taxable year in which the debt instrument is issued. The borrower and lender should attach this signed statement (or a copy thereof) to their timely filed Federal income tax returns.

(2) *Successors of electing parties.* Except as otherwise provided in this paragraph (c)(2), the cash method election under section 1274A(c) applies to any successor of the electing lender or borrower. Thus, for any period after the transfer of a cash method debt instrument, the successor takes into account the interest (including unstated interest) on the instrument under the cash receipts and disbursements method of accounting. Nevertheless, if the lender (or any successor thereof) transfers the cash method debt instrument to a taxpayer who uses an accrual method of accounting, section 1272 rather than section 1274A(c) applies to the suc-

cessor of the lender with respect to the debt instrument for any period after the date of the transfer. The borrower (or any successor thereof), however, remains on the cash receipts and disbursements method of accounting with respect to the cash method debt instrument.

(3) *Modified debt instrument.* In the case of a debt instrument issued in a debt-for-debt exchange that qualifies as an exchange under section 1001, the debt instrument is eligible for the election to be a cash method debt instrument if the other prerequisites to making the election in section 1274A(c) are met. However, if a principal purpose of the modification is to defer interest income or deductions through the use of the election, then the debt instrument is not eligible for the election.

(4) *Debt incurred or continued to purchase or carry a cash method debt instrument.* If a debt instrument is incurred or continued to purchase or carry a cash method debt instrument, rules similar to those under section 1277 apply to determine the timing of the interest deductions for the debt instrument. For purposes of the preceding sentence, rules similar to those under section 265(a)(2) apply to determine whether a debt instrument is incurred or continued to purchase or carry a cash method debt instrument.

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§ 1.1275-1 Definitions.

(a) *Applicability.* The definitions contained in this section apply for purposes of sections 163(e) and 1271 through 1275 and the regulations thereunder.

(b) *Adjusted issue price—(1) In general.* The adjusted issue price of a debt instrument at the beginning of the first accrual period is the issue price. Thereafter, the adjusted issue price of the debt instrument is the issue price of the debt instrument—

(i) Increased by the amount of OID previously includible in the gross income of any holder (determined without regard to section 1272(a)(7) and section 1272(c)(1)); and

(ii) Decreased by the amount of any payment previously made on the debt instrument other than a payment of qualified stated interest. See § 1.1275-