

this subsection and subsection (b) as if it were a debt instrument,

(B) the issue price determined for such unit shall be allocated to each element of such unit on the basis of the relationship of the fair market value of such element to the fair market value of all elements in such unit, and

(C) the issue price of any debt instrument included in such unit shall be the portion of the issue price of the unit allocated to the debt instrument under subparagraph (B).

(Added Pub. L. 98-369, div. A, title I, §41(a), July 18, 1984, 98 Stat. 536; amended Pub. L. 99-514, title XVIII, §1803(a)(10), Oct. 22, 1986, 100 Stat. 2794.)

AMENDMENTS

1986—Subsec. (b)(3)(B). Pub. L. 99-514 amended subpar. (B) generally, designating existing provisions as cl. (i) and adding cl. (ii).

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by 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

Section applicable to taxable years ending after July 18, 1984, except as otherwise provided, see section 44 of Pub. L. 98-369, set out as a note under section 1271 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 [§§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.

§ 1274. Determination of issue price in the case of certain debt instruments issued for property

(a) In general

In the case of any debt instrument to which this section applies, for purposes of this subpart, the issue price shall be—

- (1) where there is adequate stated interest, the stated principal amount, or
- (2) in any other case, the imputed principal amount.

(b) Imputed principal amount

For purposes of this section—

(1) In general

Except as provided in paragraph (3), the imputed principal amount of any debt instrument shall be equal to the sum of the present values of all payments due under such debt instrument.

(2) Determination of present value

For purposes of paragraph (1), the present value of a payment shall be determined in the manner provided by regulations prescribed by the Secretary—

- (A) as of the date of the sale or exchange, and

(B) by using a discount rate equal to the applicable Federal rate, compounded semi-annually.

(3) Fair market value rule in potentially abusive situations

(A) In general

In the case of any potentially abusive situation, the imputed principal amount of any debt instrument received in exchange for property shall be the fair market value of such property adjusted to take into account other consideration involved in the transaction.

(B) Potentially abusive situation defined

For purposes of subparagraph (A), the term “potentially abusive situation” means—

- (i) a tax shelter (as defined in section 6662(d)(2)(C)(ii)), and
- (ii) any other situation which, by reason of—

- (I) recent sales transactions,
- (II) nonrecourse financing,
- (III) financing with a term in excess of the economic life of the property, or
- (IV) other circumstances,

is of a type which the Secretary specifies by regulations as having potential for tax avoidance.

(c) Debt instruments to which section applies

(1) In general

Except as otherwise provided in this subsection, this section shall apply to any debt instrument given in consideration for the sale or exchange of property if—

- (A) the stated redemption price at maturity for such debt instrument exceeds—
 - (i) where there is adequate stated interest, the stated principal amount, or
 - (ii) in any other case, the imputed principal amount of such debt instrument determined under subsection (b), and

(B) some or all of the payments due under such debt instrument are due more than 6 months after the date of such sale or exchange.

(2) Adequate stated interest

For purposes of this section, there is adequate stated interest with respect to any debt instrument if the stated principal amount for such debt instrument is less than or equal to the imputed principal amount of such debt instrument determined under subsection (b).

(3) Exceptions

This section shall not apply to—

(A) Sales for \$1,000,000 or less of farms by individuals or small businesses

(i) In general

Any debt instrument arising from the sale or exchange of a farm (within the meaning of section 6420(c)(2))—

- (I) by an individual, estate, or testamentary trust,
- (II) by a corporation which as of the date of the sale or exchange is a small business corporation (as defined in section 1244(c)(3)), or

month in the 3-calendar-month period ending with the 1st calendar month in which there is a binding contract in writing for such sale or exchange.

(3) Term of debt instrument

In determining the term of a debt instrument for purposes of this subsection, under regulations prescribed by the Secretary, there shall be taken into account options to renew or extend.

(e) 110 Percent rate where sale-leaseback involved

(1) In general

In the case of any debt instrument to which this subsection applies, the discount rate used under subsection (b)(2)(B) or section 483(b) shall be 110 percent of the applicable Federal rate, compounded semiannually.

(2) Lower discount rates shall not apply

Section 1274A shall not apply to any debt instrument to which this subsection applies.

(3) Debt instruments to which this subsection applies

This subsection shall apply to any debt instrument given in consideration for the sale or exchange of any property if, pursuant to a plan, the transferor or any related person leases a portion of such property after such sale or exchange.

(Added Pub. L. 98-369, div. A, title I, §41(a), July 18, 1984, 98 Stat. 538; amended Pub. L. 99-121, title I, §§101(a)(1), (b), (c), 102(b), Oct. 11, 1985, 99 Stat. 505, 506, 508; Pub. L. 99-514, title XVIII, §1803(a)(14)(A), Oct. 22, 1986, 100 Stat. 2797; Pub. L. 101-239, title VII, §7721(c)(11), Dec. 19, 1989, 103 Stat. 2400; Pub. L. 104-188, title I, §1704(t)(78), Aug. 20, 1996, 110 Stat. 1891; Pub. L. 105-34, title III, §312(d)(1), Aug. 5, 1997, 111 Stat. 839; Pub. L. 115-141, div. U, title IV, §401(a)(179), Mar. 23, 2018, 132 Stat. 1193.)

AMENDMENTS

2018—Subsec. (b)(3)(B)(i). Pub. L. 115-141 substituted “section 6662(d)(2)(C)(ii)” for “section 6662(d)(2)(C)(iii)”.

1997—Subsec. (c)(3)(B). Pub. L. 105-34 substituted “section 121” for “section 1034”.

1996—Subsec. (b)(3)(B)(i). Pub. L. 104-188 substituted “section 6662(d)(2)(C)(iii)” for “section 6662(d)(2)(C)(ii)”.

1989—Subsec. (b)(3)(B)(i). Pub. L. 101-239 substituted “section 6662(d)(2)(C)(ii)” for “section 6661(b)(2)(C)(ii)”.

1986—Subsec. (c)(3)(A). Pub. L. 99-514 substituted “for \$1,000,000 or less” for “for less than \$1,000,000” in heading of subsec. (c)(4)(A) as so designated prior to its redesignation as subsec. (c)(3)(A) by Pub. L. 99-121, §101(a)(1)(D), see 1985 Amendment note below.

1985—Subsec. (b)(2)(B). Pub. L. 99-121, §101(a)(1)(A), struck out “120 percent of” after “rate equal to”.

Subsec. (c)(1)(A)(ii). Pub. L. 99-121, §101(a)(1)(B), amended cl. (ii) generally, substituting “the imputed principal amount of such debt instrument determined under subsection (b)” for “the testing amount”.

Subsec. (c)(2). Pub. L. 99-121, §101(a)(1)(C), substituted “the imputed principal amount of such debt instrument determined under subsection (b)” for “the testing amount”.

Subsec. (c)(3). Pub. L. 99-121, §101(a)(1)(D), redesignated par. (4) as (3). Former par. (3), defining “testing amount”, was struck out.

Subsec. (c)(4). Pub. L. 99-121, §102(b), added par. (4). Former par. (4) redesignated (3).

Subsec. (d)(1)(B) to (D). Pub. L. 99-121, §101(b)(1), amended subpars. (B) to (D) generally, in subpar. (B)

substituting provisions setting a monthly schedule for the determination of Federal rates for provisions which had formerly set a semi-annual schedule for the determination of such rates, in subpar. (C) substituting provisions setting a monthly schedule for the determination of Federal short-term, mid-term, and long-term rates based on the average market yield during any 1-month period ending in the month in which the determination is made for former provisions which had directed that the Federal rate determined under subpar. (A) apply during the appropriate 6-month period, and in subpar. (D) substituting provisions allowing a lower rate in certain cases for provisions relating to the setting of the Federal rate for any 6-month period.

Subsec. (d)(2). Pub. L. 99-121, §101(b)(2), amended par. (2) generally. Prior to amendment, par. (2) read as follows: “In the case of any sale or exchange, the determination of the applicable Federal rate shall be made as of the first day on which there is a binding contract in writing for the sale or exchange.”

Subsec. (e). Pub. L. 99-121, §101(c), added subsec. (e).

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105-34 applicable to sales and exchanges after May 6, 1997, with certain exceptions, see section 312(d) of Pub. L. 105-34, set out as a note under section 121 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by Pub. L. 101-239 applicable to returns the due date for which (determined without regard to extensions) is after Dec. 31, 1989, see section 7721(d) of Pub. L. 101-239, set out as a note under section 461 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by 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 1985 AMENDMENT

Pub. L. 99-121, title I, §105(a), Oct. 11, 1985, 99 Stat. 510, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by sections 101 and 102 [enacting section 1274A and amending this section and sections 280G and 483 of this title] shall apply to sales and exchanges after June 30, 1985, in taxable years ending after such date. The amendment made by section 2 of Public Law 98-612 [amending section 44(b) of Pub. L. 98-369, set out as a note under section 1271 of this title] shall not apply to sales and exchanges after June 30, 1985, in taxable years ending after such date.

“(2) REGULATORY AUTHORITY TO ESTABLISH LOWER RATE.—Section 1274(d)(1)(D) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954], as added by section 101(b), shall apply as if included in the amendments made by section 41 of the Tax Reform Act of 1984 [Pub. L. 98-369, see Effective Date note set out under section 1271 of this title].”

EFFECTIVE DATE

Section applicable to taxable years ending after July 18, 1984, and applicable to sales or exchanges after Dec. 31, 1984, but not applicable to any sale or exchange pursuant to a written contract which was binding on Mar. 1, 1984, and at all times thereafter before the sale or exchange, see section 44 of Pub. L. 98-369, set out as a note under section 1271 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 [§§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.

TRANSITIONAL RULE FOR PURPOSES OF IMPUTED
INTEREST RULES

Provisions respecting treatment of debt instruments received in exchange for property, relating to special rules for sales after Dec. 31, 1984, and before July 1, 1985, general rule for assumptions of loans, exception for assumptions of loans made on or before Oct. 15, 1984, and exception for assumptions of loans with respect to certain property, see section 44(b)(4)-(7) of Pub. L. 98-369, as amended, set out as an Effective Date note under section 1271 of this title.

§ 1274A. Special rules for certain transactions where stated principal amount does not exceed \$2,800,000

(a) Lower discount rate

In the case of any qualified debt instrument, the discount rate used for purposes of sections 483 and 1274 shall not exceed 9 percent, compounded semiannually.

(b) Qualified debt instrument defined

For purposes of this section, the term “qualified debt instrument” means any debt instrument given in consideration for the sale or exchange of property (other than new section 38 property within the meaning of section 48(b), as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) if the stated principal amount of such instrument does not exceed \$2,800,000.

(c) Election to use cash method where stated principal amount does not exceed \$2,000,000

(1) In general

In the case of any cash method debt instrument—

(A) section 1274 shall not apply, and

(B) interest on such debt instrument shall be taken into account by both the borrower and the lender under the cash receipts and disbursements method of accounting.

(2) Cash method debt instrument

For purposes of paragraph (1), the term “cash method debt instrument” means any qualified debt instrument if—

(A) the stated principal amount does not exceed \$2,000,000,

(B) the lender does not use an accrual method of accounting and is not a dealer with respect to the property sold or exchanged,

(C) section 1274 would have applied to such instrument but for an election under this subsection, and

(D) an election under this subsection is jointly made with respect to such debt instrument by the borrower and lender.

(3) Successors bound by election

(A) In general

Except as provided in subparagraph (B), paragraph (1) shall apply to any successor to the borrower or lender with respect to a cash method debt instrument.

(B) Exception where lender transfers debt instrument to accrual method taxpayer

If the lender (or any successor) transfers any cash method debt instrument to a taxpayer who uses an accrual method of accounting, this paragraph shall not apply with respect to such instrument for periods after such transfer.

(4) Fair market value rule in potentially abusive situations

In the case of any cash method debt instrument, section 483 shall be applied as if it included provisions similar to the provisions of section 1274(b)(3).

(d) Other special rules

(1) Aggregation rules

For purposes of this section—

(A) 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, and

(B) all debt instruments arising from the same transaction (or a series of related transactions) shall be treated as 1 debt instrument.

(2) Adjustment for inflation

In the case of any debt instrument arising out of a sale or exchange during any calendar year after 1989, each dollar amount contained in the preceding provisions of this section shall be increased by an amount equal to—

(A) such amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1988” for “calendar year 2016” in subparagraph (A)(ii) thereof.

Any increase under the preceding sentence shall be rounded to the nearest multiple of \$100 (or, if such increase is a multiple of \$50, such increase shall be increased to the nearest multiple of \$100).

(e) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection, including—

(1) regulations coordinating the provisions of this section with other provisions of this title,

(2) regulations necessary to prevent the avoidance of tax through the abuse of the provisions of subsection (c), and

(3) regulations relating to the treatment of transfers of cash method debt instruments.

(Added Pub. L. 99-121, title I, §102(a), Oct. 11, 1985, 99 Stat. 506; amended Pub. L. 101-508, title XI, §11813(b)(22), Nov. 5, 1990, 104 Stat. 1388-555; Pub. L. 104-188, title I, §1704(t)(62), Aug. 20, 1996, 110 Stat. 1890; Pub. L. 115-97, title I, §11002(d)(10), Dec. 22, 2017, 131 Stat. 2062.)

INFLATION ADJUSTED ITEMS FOR CERTAIN YEARS

For inflation adjustment of certain items in this section, see Revenue Rulings listed in a table below and Revenue Procedures listed in a table under section 1 of this title.