

§ 1.171-4

26 CFR Ch. I (4-1-04 Edition)

\$8,881.83, the qualified stated interest allocable to the period (\$10,000) offset with bond premium allocable to the period (\$1,118.17). The adjusted acquisition price on April 1, 2000, is \$108,881.83 (\$110,000 - \$1,118.17). For the accrual period ending on April 1, 2001, M includes in income \$8,791.54, the qualified stated interest allocable to the period (\$10,000) offset with bond premium allocable to the period (\$1,208.46). The adjusted acquisition price on April 1, 2001, is \$107,673.37 (\$108,881.83 - \$1,208.46).

(v) *Partial call.* Assume N calls one-half of M's bond for \$52,500 on April 1, 2001. Because it was assumed the call would not be exercised, the call is a change in circumstances. However, the partial call is also a pro-rata prepayment within the meaning of § 1.1275-2(f)(2). As a result, the call is treated as a retirement of one-half of the bond. Under paragraph (c)(5)(ii) of this section, M may deduct \$1,336.68, the excess of its adjusted acquisition price in the retired portion of the bond (\$107,673.37/2, or \$53,836.68) over the amount received on redemption (\$52,500). M's adjusted basis in the portion of the bond that remains outstanding is \$53,836.68 (\$107,673.37 - \$53,836.68).

[T.D. 8746, 62 FR 68180, Dec. 31, 1997, as amended by T.D. 8838, 64 FR 48547, Sept. 7, 1999]

§ 1.171-4 Election to amortize bond premium on taxable bonds.

(a) *Time and manner of making the election—(1) In general.* A holder makes the election to amortize bond premium by offsetting interest income with bond premium in the holder's timely filed federal income tax return for the first taxable year to which the holder desires the election to apply. The holder should attach to the return a statement that the holder is making the election under this section.

(2) *Coordination with OID election.* If a holder makes an election under § 1.1272-3 for a bond with bond premium, the holder is deemed to have made the election under this section.

(b) *Scope of election.* The election under this section applies to all taxable bonds held during or after the taxable year for which the election is made.

(c) *Election to amortize made in a subsequent taxable year—(1) In general.* If a holder elects to amortize bond premium and holds a taxable bond acquired before the taxable year for which the election is made, the holder may not amortize amounts that would have been amortized in prior taxable

years had an election been in effect for those prior years.

(2) *Example.* The following example illustrates the rule of this paragraph (c):

Example. (i) *Facts.* On May 1, 1999, C purchases for \$130,000 a taxable bond maturing on May 1, 2006, with a stated principal amount of \$100,000, payable at maturity. The bond provides for unconditional payments of interest of \$15,000, payable on May 1 of each year. C uses the cash receipts and disbursements method of accounting and the calendar year as its taxable year. C has not previously elected to amortize bond premium, but does so for 2002.

(ii) *Amount to amortize.* C's basis for determining loss on the sale or exchange of the bond is \$130,000. Thus, under § 1.171-1, the amount of bond premium is \$30,000. Under § 1.171-2, if a bond premium election were in effect for the prior taxable years, C would have amortized \$3,257.44 of bond premium on May 1, 2000, and \$3,551.68 of bond premium on May 1, 2001, based on annual accrual periods ending on May 1. Thus, for 2002 and future years to which the election applies, C may amortize only \$23,190.88 (\$30,000 - \$3,257.44 - \$3,551.68).

(d) *Revocation of election.* The election under this section may not be revoked unless approved by the Commissioner. Because a revocation of the election is a change in accounting method, a taxpayer must follow the rules under § 1.446-1(e)(3)(i) to request the Commissioner's consent to revoke the election. A revocation of the election applies to all taxable bonds held during or after the taxable year for which the revocation is effective. The holder may not amortize any remaining bond premium on bonds held at the beginning of the taxable year for which the revocation is effective. Therefore, no adjustment under section 481 is allowed upon the revocation of the election because no items of income or deduction are omitted or duplicated.

[T.D. 8746, 62 FR 68182, Dec. 31, 1997]

§ 1.171-5 Effective date and transition rules.

(a) *Effective date—(1) In general.* Sections 1.171-1 through 1.171-4 apply to bonds acquired on or after March 2, 1998. However, if a holder makes the election under § 1.171-4 for the taxable year containing March 2, 1998, or any subsequent taxable year, §§ 1.171-1 through 1.171-4 apply to bonds held on