The proper tax treatment of advance payments has a storied history in tax cases and IRS administrative guidance. One advance payment issue that has received significant attention from both taxpayers and the IRS over the last several years is the proper treatment of gift card income and whether taxpayers can take advantage of income deferral provisions for gift revenue.

The fact that it has become a significant issue is not surprising. Gift card revenue has exploded recently. It is estimated that there are approximately $100,000,000 in gift card sales annually with at least 3% of gift cards failing to be redeemed each year. As a result, a range of questions arise regarding the proper treatment of gift card income. Moreover, gift cards are being used in many ways further complicating consideration of when and income should be recognized and whether income deferral provisions are applicable.

This live webinar will discuss and consider the range of issues that arise with respect to gift cards. We will review IRS guidance addressing gift cards and taxpayer concerns, including when and whether an accounting method change may be used to change the timing of income recognition associated with gift cards. A related issue that the program will also address is the limited exception available for coupons issued with sales and the application of this deferral provision following the Capital One decision.

Learning Objectives:
• You will be able to discuss income deferral consideration.
• You will be able to review accounting method change considerations and strategy.
• You will be able to identify outstanding issues affecting the treatment of gift cards.

Income Recognition Overview
• Section 451 – When Does the Right to Receive Income Become Fixed? What Is the Proper Treatment of Advance Payments?
• History and Development of Controlling Authorities Addressing Deferral of Advance Payments
  – Case Law Trilogy Considers Whether IRS Could Require Advance Payments to Be Included in Income in the Year of Receipt
  – Subsequent Case Law Allows Limited Deferral in Certain Circumstances
  – Questions Arise Regarding Whether Deferral Is Permitted and If So, Length of Deferral

Income Recognition Issues Arising With Gift Card and Certificate Sales
• Accounting Method Change Considerations and Strategy
  – When Is an Accounting Method Change Required?
  – When Can a Required Method Change Be Made Automatically?
  – Are There Other Approaches to Consider When a Method Change Is Not Available?
• Outstanding Issues Affecting the Treatment of Gift Cards
  – Treas. Reg. §1.451-4 – Allows Limited Deferral Via Accelerated Deduction for the Estimated Future Costs of Redeeming Coupons Issued With Sales
  – Capital One – Considering Whether Credit Card Issuer Could Take Advantage of Deferral Provision
    • Application to Corporate Reward Programs
  – Additional Types of Gift Cards

Ellen McElroy
Pepper Hamilton LLP

• Partner with Pepper Hamilton LLP, resident in the Washington, D.C. office
• Focuses on a broad variety of corporate tax issues, primarily accounting method considerations
• Regularly advises clients on the proper tax treatment of costs associated with tangible property, (including the treatment of repair costs), intangible property (including acquisition costs and recovery), and corporate transaction costs
• With respect to corporate transaction costs, she advises clients regarding various corporate transactions, including both acquisitive and divisive transactions, both strategic and private equity transactions

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Tax Treatment of Gift Card and Certificate Sales

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