

## Part I

### Section 451–General Rule for Taxable Year of Inclusion

26 CFR 1.451-1: Taxable Year of Inclusion  
(Also: §§ 61, 446)

Rev. Rul. 2004-52

## ISSUES

(1) Are credit card annual fees interest for federal income tax purposes?

(2) When are credit card annual fees includible in gross income by the card issuer?

## FACTS

X, a taxpayer that uses an overall accrual method of accounting for federal income tax purposes, issues credit cards. Each card allows the cardholder to access a revolving line of credit to make purchases of goods and services and, if otherwise provided for under the applicable cardholder agreement, to obtain cash advances.

Credit card issuers, including X, charge certain cardholders an annual fee. These credit card issuers make various benefits and services available to their cardholders during the year, regardless of whether the cardholder actually utilizes them. Further, although they provide these benefits and services to cardholders, no part of the annual fee that is charged to any cardholder is for a specific benefit or service provided by a credit card issuer to that cardholder.

Each cardholder's credit card agreement sets forth the applicable terms and conditions under which X may charge that cardholder an annual fee. X charges some cardholders a nonrefundable annual fee. X charges other cardholders an annual fee that is refundable on a pro rata basis if the cardholder closes the account during the period covered by the fee.

Under the applicable cardholder agreement, no annual fee becomes due and payable until X posts an annual fee charge to the cardholder's credit card account. X reflects this posting in the cardholder's credit card statement. X generally posts the full amount of the annual fee in a single charge unless the terms of the agreement require X to post the annual fee charge in installments.

## LAW AND ANALYSIS

For federal income tax purposes, interest is an amount that is paid in compensation for the use or forbearance of money. Deputy v. DuPont, 308 U.S. 488 (1940), 1940-1 C.B. 118; Old Colony Railroad Co. v. Commissioner, 284 U.S. 552 (1932), 1932-1 C.B. 274. Neither the label used for the fee nor a taxpayer's treatment of the fee for financial or regulatory reporting purposes is determinative of the proper federal income tax characterization of that fee. See Thor Power Tool Co. v. Commissioner, 439 U.S. 522, 542-43 (1979), 1979-1 C.B. 167, 174-75; Rev. Rul. 72-315, 1972-1 C.B. 49.

The annual fee that credit card issuers, including X, charge any cardholder is not for any specific benefit provided by the credit card issuer to that cardholder. Rather, it is charged for all of the benefits and services that are available to the cardholder under the applicable cardholder agreement. Because cardholders pay annual fees to credit card issuers, including X, in return for all of the benefits and services available under the applicable credit card agreement, annual fees are not compensation for the use or forbearance of money. Thus, X's annual fee income is not interest income for federal income tax purposes.

Under § 451(a) of the Internal Revenue Code, the amount of any item of gross income is includible in gross income for the taxable year in which it is received by the taxpayer, unless that amount is to be properly accounted for in a different period under the method of accounting used by the taxpayer in computing taxable income.

Under § 1.451-1(a) of the Income Tax Regulations, income is includible in gross income by a taxpayer that uses an accrual method of accounting when all events have occurred that fix the taxpayer's right to receive that income and the amount of that income can be determined with reasonable accuracy. See also § 1.446-1(c)(1)(ii)(A). Generally, all the events that fix the right to receive income occur when either the required performance takes place, payment is due, or payment is made, whichever occurs first (the all events test). See Rev. Rul. 2003-10, 2003-3 I.R.B. 288; Rev. Rul. 80-308, 1980-2 C.B. 162.

X is required to include these annual fees in gross income under § 1.451-1(a) when the fee income becomes due and payable under its agreements, because X's right to the income is fixed at that point and the amount of the income can be determined with reasonable accuracy. Thus, the all events test is satisfied when X posts an annual fee charge to a cardholder's credit card account even if X later is required to refund a portion of a previously posted refundable annual fee charge because the cardholder closes the account during the period covered by that fee.

Notwithstanding the holding of this revenue ruling, Rev. Proc. 2004-32, 2004-22 I.R.B. dated June 1, 2004, this bulletin, allows card issuers to account for annual fee

income using the Ratable Inclusion Method for Credit Card Annual Fees, which is described in section 4 of that revenue procedure. Rev. Proc. 2004-32 also provides automatic consent for a taxpayer described in this revenue ruling to change its method of accounting for annual fee income.

## HOLDINGS

(1) Credit card annual fees are not interest for federal income tax purposes.

(2) Credit card annual fees are includible in gross income by the card issuer when they become due and payable by cardholders under the terms of the credit card agreements.

## DRAFTING INFORMATION

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