The Lure of a Sec. 475 Election

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Prudence is in order any time a taxpayer considers an election under the Internal Revenue Code. When it comes to Sec. 475, this axiom is especially relevant. Sec. 475 permits mark-to-market accounting for eligible taxpayers, which is a substantial deviation from the Code's traditional standard of income recognition only when it is realized. More specifically, the election requires income recognition at the end of each year based on increases and decreases in fair market values. A Sec. 475 election can yield tremendous tax benefits with few downside risks; however, taxpayers must be wary of its potential pitfalls.