1999 Income Tax School

FORM 4797

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1999 Income Tax School

FORM 4797

Form 4797 is used primarily to report gains and losses from the disposition of business-use assets, gains, and losses from certain involuntary conversions and recapture amounts under I.R.C. §§179 and 280F(b)(2).

Generally, reporting on Form 4797 is advantageous to the taxpayer because:

1. Gain reported on Form 4797 is normally not subject to self-employment tax.
2. Some of the gains reported on Form 4797 are treated as long-term capital gain.

I.R.C. §1231 TREATMENT

One of the primary functions of Form 4797 is to aggregate gains and losses from I.R.C. §1231 transactions. If there is a net gain from these transactions, all of the gains and losses are treated as long-term capital gains and losses. If there is a net loss, all of the gains and losses are treated as ordinary income and losses.

To qualify for I.R.C. §1231 treatment [I.R.C. §1231(a)(3)], property must be either:

1. Property "used in a trade or business" (for example, land, buildings, and equipment) or
2. Property that was subject to an involuntary conversion (defined below) and was:
   a. Property used in the trade or business, or
   b. A capital asset that was held for more than a year in connection with a trade or business or a transaction entered into for profit.

Practitioner Note. Although land, buildings, and equipment that are used in a business are commonly referred to as capital assets, I.R.C. §1221(2) excludes such assets from the definition of "capital assets."

PROPERTY USED IN A TRADE OR BUSINESS: GENERAL DEFINITION

In the context of I.R.C. §1231, the phrase **"used in the trade or business"** has a very specific meaning [I.R.C. §1231(b)]. Property must meet **three requirements** to be "used in the trade or business" under this definition:

1. It must be **held for more than one year,**
2. It must be used in a trade or business (in the normal meaning of that phrase as used in I.R.C. §162) and be either:
   a. **subject to the allowance for depreciation,** or
   b. **real property,** and

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3. It cannot be inventory or property that is held for sale in the ordinary course of business.

Practitioner Note. Generally, case law indicates that rental real estate is an I.R.C. §1231 asset and not §1221 investment property.

Example 1. Scott Weiland's only I.R.C. §1231 transaction for 1999 was the sale of land used in his business. He purchased the land on October 20, 1963, for $20,000. He sold it on November 8, 1999, for $30,000 and paid his broker a $1,400 commission. Scott should report the sale as shown on Form 4797.

Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property
(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))
► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184
1999
Attachment Sequence No. **27**

Name(s) shown on return: *Scott Weiland (Example 1)*

Identifying number: *111 22 4444*

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 1

Part I **Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year**

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2	*land*	*10/20/63*	*11/08/99*	*30,000*		*21,400*	*8,600*

3	Gain, if any, from Form 4684, line 39	3	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6	Gain, if any, from line 32, from other than casualty or theft	6	
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	7	*8,600*

Proof as of 5/4/1999

INVOLUNTARY CONVERSIONS

The involuntary conversions for purposes of I.R.C. §1231 include conversions in any one of the following three groups:

1. Destruction by fire, storm, shipwreck, or other casualty, but only if the recognized gains from such conversions exceed the recognized losses from such conversions;
2. Theft or seizure, but only if the recognized gains from such conversions exceed the recognized losses from such conversions; or
3. Condemnation or the threat or imminence of condemnation.

Practitioner Note. The gain or loss from involuntary conversions is excluded from I.R.C. §1231 treatment if:

- The involuntary conversion is due to fire, storm, shipwreck, or other casualty, or from theft, **and**
- The losses from such conversion exceed the gains from such conversion for the taxable year.

Example 2. On July 10, 1999, the city acquired by condemnation 10 acres of vacant land from Teresa Parks to build a new street. Teresa purchased the land on December 13, 1991, for $100,000 as an invest-

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ment. She paid an attorney $5,000 to represent her in the eminent domain proceeding. She received $75,000 from the city. Teresa should report the transaction as shown on the following Form 4797.

Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return: ***Teresa Parks (Example 2)***

Identifying number: ***123 45 6789***

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 1

Part I **Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year**

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2	*land*	*12/13/91*	*7/10/99*	*75,000*		*105,000*	*-30,000*

3	Gain, if any, from Form 4684, line 39	3	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6	Gain, if any, from line 32, from other than casualty or theft	6	
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: **Partnerships—**Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below. **S corporations—**Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. **All others—**If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	*-30,000*
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	8	
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line(s) as follows (see instructions): **S corporations—**Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. **All others—**If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.	9	

Part II **Ordinary Gains and Losses**

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11	Loss, if any, from line 7	11	(*30,000*)
12	Gain, if any, from line 7 or amount from line 8, if applicable	12	
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	*-30,000*
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.		
b	For individual returns:		
(1)	If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	18b(1)	
(2)	Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	*-30,000*

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OTHER EXCLUDED PROPERTY

Other property that is specifically excluded from I.R.C. §1231 treatment includes:

1. **A copyright; a literary, musical, or artistic composition; a letter, memorandum,** or similar property [I.R.C. §1231(b)(1)(C)] held by:
   - **a.** A taxpayer whose personal efforts created the property,
   - **b.** In the case of a letter, memorandum, or similar property, a taxpayer for whom the property was prepared or produced, or
   - **c.** A taxpayer who acquired the property from a taxpayer described in *a* or *b* above in a transaction that gave him or her a carryover basis in the property.
2. A **publication of the United States government** that is received from the United States government, or any agency of it, other than by purchase at the price at which it is offered for sale to the public [I.R.C. §1231(b)(1)(D)], and that is held by:
   - **a.** A taxpayer who received the publication from the United States government, or
   - **b.** A taxpayer who acquired the property from a taxpayer described in *a* above, in a transaction that gave him or her a carryover basis in the property.

OTHER INCLUDED PROPERTY

Other property that is specifically included in I.R.C. §1231 property.

1. Timber for which the owner has made the election under I.R.C. §631(a) to treat the cutting as a sale or exchange [I.R.C. §1231(b)(2)],
2. Timber, coal, or domestic iron ore sold under a contract that retains an economic interest for the taxpayer [I.R.C. §1231(b)(2)],
3. Cattle and horses held for draft, breeding, dairy, or sporting purposes and held for 24 months or more [I.R.C. §1231(b)(3)],
4. Other livestock held for draft, breeding, dairy, or sporting purposes and held for 12 months or more [I.R.C. §1231(b)(3)(B)], and
5. Unharvested crops [I.R.C. §1231(b)(4)] that are:
   - **a.** On land used in the trade or business that has been held for more than one year, and
   - **b.** Sold or exchanged at the same time and to the same person as the land.

RECAPTURE OF I.R.C. §1231 LOSSES FROM PRIOR YEARS

Code §1231(c) adds another issue that is dealt with in Part I of Form 4797. The issue is that net I.R.C. §1231 gains in a given year must be reported as ordinary income to the extent that I.R.C. §1231 losses were deducted against ordinary income in the previous five years and have not been recaptured. The term recapture refers to the recharacterization of I.R.C. §1231 gains (which would normally be treated as long-term capital gain) as ordinary income. This rule requires a taxpayer to keep a running balance of unrecaptured I.R.C. §1231 losses so that the amount of net I.R.C. §1231 gain that must be reported as ordinary income can be calculated.

Example 3. Shane Soldinger had the following I.R.C. §1231 gains and losses:

Year	Gain (Loss)
1994	$(10,000)
1995	(10,000)
1996	15,000
1997	10,000
1998	(7,000)

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In 1999 Shane had $10,000 of I.R.C. §1231 gain. He calculates his recapture as follows:

Year	Gain (Loss)	Loss Recapture	Unrecaptured Loss Remaining
1994	$(10,000)	-0-	$(10,000)
1995	(10,000)	-0-	(20,000)
1996	15,000	$15,000	(5,000)
1997	10,000	5,000	-0-
1998	(7,000)	-0-	(7,000)
1999		7,000	-0-

The five-year look-back recapture rule is applied by comparing the net I.R.C. §1231 gain with the unrecaptured I.R.C. §1231 losses from the previous five years. Shane's $15,000 net gains in 1996 and $10,000 in 1997 caused him to recapture all of the $20,000 net losses from 1994 and 1995. Therefore, his only unrecaptured losses that are carried to 1999 are the $7,000 of net losses from 1998. Those unrecaptured losses cause Shane to **recognize $7,000 of his $10,000 net I.R.C. §1231 gain in 1999 as ordinary income. The remaining $3,000 is long-term capital gain.**

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Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return: ***Shane Soldinger (Example 3)***

Identifying number: ***123 45 6789***

7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: **Partnerships—**Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below. **S corporations—**Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. **All others—**If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	*10,000*
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	8	*7,000*
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line(s) as follows (see instructions): **S corporations—**Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. **All others—**If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.	9	*3,000*

Part II Ordinary Gains and Losses

10	Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):		
11	Loss, if any, from line 7	11	( )
12	Gain, if any, from line 7 or amount from line 8, if applicable	12	*7,000*
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	*7,000*
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.		
b	For individual returns:		
(1)	If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	18b(1)	
(2)	Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	*7,000*

CASUALTY LOSSES

A casualty is the damage, destruction, or loss of property resulting from an unforeseen event that is sudden, unexpected, or unusual–for example, fires, thefts, storms, floods, tornadoes, vandalism, earthquakes, and other accidents.

Example 4. As a result of a flood, Bradford Cook's equipment acquired 7/1/69 and used in his business was destroyed. The equipment had a FMV of $15,000 before the flood but had been fully depreciated, resulting in a zero basis. He received $15,000 from the insurance company for the loss of the equipment. He decided not to replace the equipment. Bradford realized a $15,000 gain as a result of receiving $15,000 from the insurance company for his zero-basis equipment. He cannot defer the gain because he did not replace the equipment. Bradford reports the $15,000 as shown on the following Form 4684 and Form 4797.

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Practitioner Note. The $15,000 gain is subject to the I.R.C. §1245 recapture rules and must be reported as ordinary income on Form 4797. Note that the $15,000 gain is carried from line 22 of Form 4684 to Part III of Form 4797. The zero capital gain from line 32 of Form 4797 is carried back to line 33 of Form 4684.

Form 4684 (1999) Attachment Sequence No. **26** Page **2**

Name(s) shown on tax return. Do not enter name and identifying number if shown on other side. **Bradford Cook (Example 4)** | Identifying number **123 45 6789**

SECTION B—Business and Income-Producing Property

Part I Casualty or Theft Gain or Loss (Use a separate Part I for each casualty or theft.)

19 Description of properties (show type, location, and date acquired for each):
Property **A** *equipment 7/01/69*
Property **B**
Property **C**
Property **D**

		Properties (Use a separate column for each property lost or damaged from one casualty or theft.) A	B	C	D
20	Cost or adjusted basis of each property	20 *0*			
21	Insurance or other reimbursement (whether or not you filed a claim). See the instructions for line 3. **Note:** *If line 20 is **more than** line 21, skip line 22.*	21 *15,000*			
22	Gain from casualty or theft. If line 21 is **more than** line 20, enter the difference here and on line 29 or line 34, column (c), except as provided in the instructions for line 33. Also, skip lines 23 through 27 for that column. See the instructions for line 4 if line 21 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year.	22 *15,000*			
23	Fair market value **before** casualty or theft	23			
24	Fair market value **after** casualty or theft	24			
25	Subtract line 24 from line 23	25			
26	Enter the **smaller** of line 20 or line 25. **Note:** *If the property was totally destroyed by casualty or lost from theft, enter on line 26 the amount from line 20.*	26			
27	Subtract line 21 from line 26. If zero or less, enter -0-	27			

28 Casualty or theft loss. Add the amounts on line 27. Enter the total here and on line 29 **or** line 34 (see instructions). 28

Part II Summary of Gains and Losses (from separate Parts I)

(a) Identify casualty or theft	(b) Losses from casualties or thefts (i) Trade, business, rental or royalty property	(b) Losses from casualties or thefts (ii) Income-producing and employee property	(c) Gains from casualties or thefts includible in income
Casualty or Theft of Property Held One Year or Less			
29	( )	( )	
	( )	( )	
30 Totals. Add the amounts on line 29	30 ( )	( )	
31 Combine line 30, columns (b)(i) and (c). Enter the net gain or (loss) here and on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions		31	
32 Enter the amount from line 30, column (b)(ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040), line 27, and enter the amount from property used as an employee on Schedule A (Form 1040), line 22. Estates and trusts, partnerships, and S corporations, see instructions		32	
Casualty or Theft of Property Held More Than One Year			
33 Casualty or theft gains from Form 4797, line 32		33	*0*
34	( )	( )	

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Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► **Attach to your tax return.** ► **See separate instructions.**

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return: ***Bradford Cook (Example 4)***

Identifying number ***123 45 6789***

Proof as of 5/24/1999

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 . . . . . **1**

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2							

3 Gain, if any, from Form 4684, line 39 . . . . . **3**

4 Section 1231 gain from installment sales from Form 6252, line 26 or 37 . . . . . **4**

5 Section 1231 gain or (loss) from like-kind exchanges from Form 8824 . . . . . **5**

6 Gain, if any, from line 32, from other than casualty or theft **6**

7 Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: **7**

Partnerships—Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below.

S corporations—Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax.

All others—If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.

8 Nonrecaptured net section 1231 losses from prior years (see instructions) **8**

9 Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line(s) as follows (see instructions): **9**

S corporations—Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below.

All others—If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11 Loss, if any, from line 7 . . . . . **11** ( )

12 Gain, if any, from line 7 or amount from line 8, if applicable **12**

13 Gain, if any, from line 31 . . . . . **13** ***15,000***

14 Net gain or (loss) from Form 4684, lines 31 and 38a **14**

15 Ordinary gain from installment sales from Form 6252, line 25 or 36 . . . . . **15**

16 Ordinary gain or (loss) from like-kind exchanges from Form 8824 . . . . . **16**

17 Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions) **17**

18 Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows: **18**

a For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.

b For individual returns:

(1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions . . . . . **18b(1)**

(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14 . . . . . **18b(2)**

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Part III **Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255**

	19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A	*Equipment (from line 22 of Form 4684)*	*7/01/69*	*5/15/99*
B			
C			
D			

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20 Gross sales price (**Note:** *See line 1 before completing.*)	20	*15,000*			
21 Cost or other basis plus expense of sale	21	*18,000*			
22 Depreciation (or depletion) allowed or allowable	22	*18,000*			
23 Adjusted basis. Subtract line 22 from line 21	23	*0*			
24 Total gain. Subtract line 23 from line 20	24	*15,000*			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	*18,000*			
b Enter the **smaller** of line 24 or 25a	25b	*15,000*			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975 (see instructions)	26a				
b Applicable percentage multiplied by the **smaller** of line 24 or line 26a (see instructions)	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the **smaller** of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage (see instructions)	27b				
c Enter the **smaller** of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs (see instructions)	28a				
b Enter the **smaller** of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126 (see instructions)	29a				
b Enter the **smaller** of line 24 or 29a (see instructions)	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	*15,000*
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	*15,000*
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	*0*

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** (See instructions.)

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		

Proofs of 5/24/1999

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I.R.C. §1245 RECAPTURE

I.R.C. §1245 requires the **lesser** of the gain realized or the depreciation previously claimed to be reported as ordinary income upon sale or other transfer of an asset that is defined as §1245 property. In general, this includes personal property for which depreciation was allowed and certain real property, such as single-purpose agricultural and horticultural structures and property used as an integral part of production.

Since the gain is subject to I.R.C. §1245 recapture, the transaction is reported in Part III of Form 4797. Since all of the gain is ordinary income, it is all reported on line 13 of Form 4797.

For purposes of this provision, the following (in addition to regular depreciation) are treated as depreciation:

1. Any amount claimed as a deduction under I.R.C. §179
2. Any basis reduction as a result of discharge of indebtedness under I.R.C. §108
3. The basis reduction from claiming the investment credit [I.R.C. §50(c)(4)(a)]
4. The deduction for qualified clean-fuel vehicle property or refueling property
5. Deductions claimed under I.R.C. §190 (removal of architectural and transportation barriers to the handicapped and elderly), §193 (deduction for tertiary injectant expenses), or §1253(d)(2) or (3) (transfers of franchises, trademarks, and trade names) (as in effect before the Omnibus Reconciliation Act of 1993)

Example 5. Erika Gibbs sold a building that she used in her trade or business on February 13, 1999, for $40,000. She incurred $1,500 of expenses to sell the building. She purchased the building on June 30, 1985, for $35,000 and claimed $24,150 of ACRS accelerated depreciation. Since she claimed accelerated depreciation on nonresidential real property, the building is subject to I.R.C. §1245 recapture and must be reported in Part III of Form 4797. However, the gain on sale exceeds the depreciation claimed. The gain in excess of depreciation claimed is I.R.C. §1231 gain and is carried from line 32 to line 6 of Form 4797.

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Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return

Erika Gibbs (Example 5)

Identifying number ***123 45 6789***

Proof as of 5/24/1999

1	Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20	1	

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2							

3	Gain, if any, from Form 4684, line 39	3	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6	Gain, if any, from line 32, from other than casualty or theft	6	*3,500*
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	7	*3,500*
	Partnerships—Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below.		
	S corporations—Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax.		
	All others—If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.		
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	8	
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line(s) as follows (see instructions):	9	
	S corporations—Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below.		
	All others—If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.		

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11	Loss, if any, from line 7	11	( )
12	Gain, if any, from line 7 or amount from line 8, if applicable	12	*24,150*
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	*24,150*
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.		
b	For individual returns:		
(1)	If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	18b(1)	
(2)	Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	*24,150*

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Part III **Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255**

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A *building*	*6/30/85*	*2/13/99*
B		
C		
D		

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20 Gross sales price (**Note:** *See line 1 before completing.*)	20	*40,000*			
21 Cost or other basis plus expense of sale	21	*36,500*			
22 Depreciation (or depletion) allowed or allowable	22	*24,150*			
23 Adjusted basis. Subtract line 22 from line 21	23	*12,350*			
24 Total gain. Subtract line 23 from line 20	24	*27,650*			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	*24,150*			
b Enter the **smaller** of line 24 or 25a	25b	*24,150*			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975 (see instructions)	26a				
b Applicable percentage multiplied by the **smaller** of line 24 or line 26a (see instructions)	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the **smaller** of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage (see instructions)	27b				
c Enter the **smaller** of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs (see instructions)	28a				
b Enter the **smaller** of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126 (see instructions)	29a				
b Enter the **smaller** of line 24 or 29a (see instructions)	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	*27,650*
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	*24,150*
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	*3,500*

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** (See instructions.)

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		

Proof #5 of 5/24/1999

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DEPRECIATION RECAPTURE FROM A LIKE-KIND EXCHANGE

Gain that is recognized from a like-kind exchange of property is subject to the same recapture rules as gain recognized from the sale of the property.

Gain that is recognized from the exchange of I.R.C. §1245 property is ordinary income to the extent of depreciation claimed on the property. Gain in excess of the depreciation claimed is I.R.C. §1231 gain.

Gain that is recognized from the exchange of I.R.C. §1250 property is ordinary income to the extent that depreciation claimed on the property exceeds straight-line depreciation. The remaining gain is I.R.C. §1231 gain.

Practitioner Note. If the I.R.C. §1231 gain from the §1250 property is treated as long-term capital gain, the gain due to straight-line depreciation is subject to the 25% maximum capital gains rate. The gain in excess of depreciation claimed is subject to the 20% maximum capital gain rate.

Example 6. In 1997, Rachel Brown traded a combine with an adjusted basis of $22,000 and FMV of $40,000 for a corn planter with a FMV of $25,000, and she received $15,000 in boot. The trade qualifies as a like-kind exchange since the combine and corn planter are both included in SIC product class 3523, Farm Machinery and Equipment. The gain realized on the exchange is:

Trade-in value of combine	$40,000
Adjusted basis of combine	22,000
Gain realized	$18,000
Gain recognized (boot)	$15,000

Practitioner Note. Gain recognized is limited to the lesser of gain realized or boot received. In this case $15,000 boot was received; therefore, the deferred gain is $3,000 ($18,000–$15,000), which is recognized upon disposition of the planter.

Rachel reported the exchange on Form 8824 and Form 4797 as shown below.

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Form **8824**

Department of the Treasury
Internal Revenue Service

Like-Kind Exchanges

(and nonrecognition of gain from conflict-of-interest sales)

► See separate instructions. ► Attach to your tax return.
► Use a separate form for each like-kind exchange.

OMB No. 1545-1190

1997

Attachment Sequence No. **49**

Name(s) shown on tax return: ***Rachel Brown (Example 6)***

Identifying number: ***882 46 1031***

Part I Information on the Like-Kind Exchange

Note: *If the property described on line 1 or line 2 is real or personal property located outside the United States, indicate the country.*

1 Description of like-kind property given up ► ***combine***

2 Description of like-kind property received ► ***corn planter***

Part III Realized Gain or (Loss), Recognized Gain, and Basis of Like-Kind Property Received

Caution: *If you transferred **and** received **(a)** more than one group of like-kind properties, or **(b)** cash or other (not like-kind property, see **Reporting of multi-asset exchanges** in the instructions.*

Note: *Complete lines 12 through 14 ONLY if you gave up property that was not like-kind. Otherwise, go to line 15.*

Fair market value (FMV) of other property given up	12		
Adjusted basis of other property given up	13		
Gain or (loss) recognized on other property given up. Subtract line 13 from line 12. Report the gain or (loss) in the same manner as if the exchange had been a sale	14		
Cash received, FMV of other property received, plus net liabilities assumed by other party, reduced (but not below zero) by any exchange expenses you incurred. See instructions	15		***15,000***
FMV of like-kind property you received	16		***25,000***
Add lines 15 and 16	17		***40,000***
Adjusted basis of like-kind property you gave up, net amounts paid to other party, plus any exchange expenses **not** used on line 15. See instructions	18		***22,000***
Realized gain or (loss). Subtract line 18 from line 17	19		***18,000***
Enter the smaller of line 15 or line 19, but not less than zero	20		***15,000***
Ordinary income under recapture rules. Enter here and on Form 4797, line 16. See instructions	21		***15,000***
Subtract line 21 from line 20. If zero or less, enter -0-. If more than zero, enter here and on Schedule D or Form 4797, unless the installment method applies. See instructions	22		***0***
Recognized gain. Add lines 21 and 22	23		***15,000***
Deferred gain or (loss). Subtract line 23 from line 19. If a related party exchange, see instructions	24		***3,000***
Basis of like-kind property received. Subtract line 15 from the sum of lines 18 and 23	25		***22,000***

Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184

1997

Attachment Sequence No. **27**

Name(s) shown on return: ***Rachel Brown (Example 6)***

Identifying number: ***882 46 1031***

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11	Loss, if any, from line 7, column (g)	11	
12	Gain, if any, from line 7, column (g) or amount from line 8, column (g) if applicable	12	
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	***15,000***

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Rachel used the planter in 1997, 1998, and 1999 and then sold it for $24,000. Upon sale of the planter, she must report the following gain:

Amount realized		$24,000
Less adjusted basis:		
Unadjusted basis	$22,000	
Depreciation	8,218	
Adjusted basis		13,782
Gain realized		$10,218

Of the gain realized on the planter, $8,218 must be reported as recapture of depreciation on the planter. **The remaining $2,000 of gain realized must also be reported as depreciation recapture** since it is included in the $3,000 of gain rolled over from the combine and would have been reported as depreciation recapture if the gain had been recognized.

The taxpayer is required to include the depreciation claimed on property transferred in a like-kind exchange for the property that is currently being sold. However, the depreciation that must be included from the transferred asset is limited to the gain that is rolled over into the asset acquired—in this case, $3,000. The depreciation reported on line 22 of Form 4797 is

Depreciation on planter	$ 8,218
Deferred gain from combine	3,000
Total	$11,218

Rachel is also allowed to increase the basis she reports on line 21 of Form 4797 ($22,000 + $3,000 of deferred gain from the combine). The adjustment is necessary to arrive at the appropriate gain on line 24 of Form 4797 of $10,218.

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Part III **Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255**

19 **(a)** Description of section 1245, 1250, 1252, 1254, or 1255 property:	**(b)** Date acquired (mo., day, yr.)	**(c)** Date sold (mo., day, yr.)
A *corn planter*	*3/10/97*	*6/20/99*
B		
C		
D		

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20 Gross sales price (**Note:** *See line 1 before completing.*)	20	*24,000*			
21 Cost or other basis plus expense of sale	21	*25,000*			
22 Depreciation (or depletion) allowed or allowable	22	*11,218*			
23 Adjusted basis. Subtract line 22 from line 21	23	*13,782*			
24 Total gain. Subtract line 23 from line 20	24	*10,218*			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	*11,218*			
b Enter the **smaller** of line 24 or 25a	25b	*10,218*			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975 (see instructions)	26a				
b Applicable percentage multiplied by the **smaller** of line 24 or line 26a (see instructions)	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the **smaller** of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership.					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage (see instructions)	27b				
c Enter the **smaller** of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs (see instructions)	28a				
b Enter the **smaller** of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126 (see instructions)	29a				
b Enter the **smaller** of line 24 or 29a (see instructions)	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	*10,218*
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	*10,218*
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6, column (g), and if applicable, column (h)	32	*0*

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** See instructions.

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		

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INSTALLMENT SALES

Under the installment method, the taxpayer reports gain on a sale as payments are received, instead of reporting all the gain in the year of sale. A sale qualifies as an installment sale even if only one payment is to be received, if that payment is made after the close of the year of sale.

The portion of the payment that is income to the taxpayer is equal to the installment payments received times the gross profit ratio.

Example 7. Joe Smith sells land used in business for a gross profit of $2,000 at a contract price of $8,000. He received a $1,000 down payment in 1999. The gross profit ratio is 25% ($2,000 ÷ $8,000). Therefore, 25% of each payment collected on the sale (including the down payment) is gain and must be included in gross income for the tax year in which it's collected. The ratio remains constant for all installment payments received on the sale.

The payment is reported on Form 6252, and the gain is carried to line 4 of Form 4797 as shown below.

Form **6252**

Department of the Treasury
Internal Revenue Service

Installment Sale Income

► See separate instructions. ► Attach to your tax return.
► Use a separate form for each sale or other disposition of property on the installment method.

OMB No. 1545-0228

1999

Attachment Sequence No. **79**

Name(s) shown on return: *Joe Smith (Example 7)*

Identifying number: *123 45 6789*

1	Description of property ► *land*			
2a	Date acquired (month, day, year) ► *3 / 03 / 95*	b Date sold (month, day, year) ► *6 / 01 / 98*		
3	Was the property sold to a related party after May 14, 1980? See instructions. If "No," skip line 4 . . .		☐ Yes	☒ No
4	Was the property you sold to a related party a marketable security? If "Yes," complete Part III. If "No," complete Part III for the year of sale and the 2 years after the year of sale . . .		☐ Yes	☐ No

Part I **Gross Profit and Contract Price.** Complete this part for the year of sale only.

5	Selling price including mortgages and other debts. **Do not** include interest whether stated or unstated			5	*8,000*
6	Mortgages and other debts the buyer assumed or took the property subject to, but not new mortgages the buyer got from a bank or other source .	6			
7	Subtract line 6 from line 5 . . .	7	*8,000*		
8	Cost or other basis of property sold . . .	8	*6,000*		
9	Depreciation allowed or allowable . . .	9			
10	Adjusted basis. Subtract line 9 from line 8 . . .	10	*6,000*		
11	Commissions and other expenses of sale. . . .	11			
12	Income recapture from Form 4797, Part III. See instructions . .	12			
13	Add lines 10, 11, and 12 . . .			13	*6,000*
14	Subtract line 13 from line 5. If zero or less, **stop here. Do not** complete the rest of this form .			14	*2,000*
15	If the property described on line 1 above was your main home, enter the amount of your excluded gain. Otherwise, enter -0-. See instructions . . .			15	*0*
16	**Gross profit.** Subtract line 15 from line 14 . . .			16	*2,000*
17	Subtract line 13 from line 6. If zero or less, enter -0- . . .			17	*0*
18	**Contract price.** Add line 7 and line 17 . . .			18	*8,000*

Part II **Installment Sale Income.** Complete this part for the year of sale **and** any year you receive a payment or have certain debts you must treat as a payment on installment obligations.

19	Gross profit percentage. Divide line 16 by line 18. For years after the year of sale, see instructions			19	*25.0000*
20	**For year of sale only:** Enter amount from line 17 above; otherwise, enter -0- . . .			20	*0*
21	Payments received during year. See instructions. **Do not** include interest whether stated or unstated			21	*1,000*
22	Add lines 20 and 21 . . .			22	*1,000*
23	Payments received in prior years. See instructions. **Do not** include interest whether stated or unstated . . .	23			
24	**Installment sale income.** Multiply line 22 by line 19 . . .			24	*250*
25	Part of line 24 that is ordinary income under recapture rules. See instructions . . .			25	
26	Subtract line 25 from line 24. Enter here and on Schedule D or Form 4797. See instructions .			26	*250*

Proof as of 6/19/1999

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Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► Attach to your tax return. ► See separate instructions.

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return: *Joe Smith (Example 7)*

Identifying number: *123 45 6789*

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 1

Part I **Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year**

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2							

3	Gain, if any, from Form 4684, line 39	3	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	*250*
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6	Gain, if any, from line 32, from other than casualty or theft	6	
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	7	*250*

Proof as of 1/4/1999

TRADE-IN OF MACHINERY FOR A LEASING ARRANGEMENT

Example 8. On February 13, 1999, Spencer McDonald traded his tractor (tractor A) for a five-year lease of a new tractor (tractor B). He had purchased tractor A for $50,000 on March 3, 1985, and has fully depreciated it. The lease calls for a $17,500 payment each year for the five years. Spencer was given a credit of $15,000 against the first lease payment in exchange for tractor A and paid the remaining $2,500 in cash. Spencer is allowed to purchase tractor B at the end of the lease for a price determined by the market value of used tractors at the time of the purchase.

Question 8A. *Is Spencer allowed to deduct the $15,000 credit as a lease payment made by trading in his old tractor?*

Answer 8A. Yes. Spencer can claim a deduction for the value of the tractor he traded in as long as the arrangement is a true lease arrangement and not a disguised installment sale. The facts of this case appear to indicate a true lease.

Question 8B. *Must Spencer report any income as a result of trading in his tractor?*

Answer 8B. Yes. Spencer is treated as if he sold his tractor for $15,000 and paid that amount to the dealer in lease payments. Therefore, he must report his gain $15,000 – 0 = $15,000 in Part III of Form 4797. Since the gain is less than the depreciation he has claimed on tractor A, all of the gain is recaptured as ordinary income under I.R.C. §1245.

Practitioner Note. If the rent credit is spread out over the term of the lease, the gain is still recognized at the time of disposition. The rent credit is deductible in the year of application.

Example 9. Assume that Spencer's arrangement with his dealer was as follows. The lease payments for tractor B are set by subtracting the $15,000 trade-in value of tractor A from the $70,000 list price of

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tractor B and amortizing the remaining $55,000 over five years at a 7% interest rate. At the end of the lease, Spencer is allowed to keep the tractor.

Question 9. *Does Spencer report the transaction in the same manner as described above?*

Answer 9. No. The arrangement is now a like-kind exchange and an installment purchase/sale. Therefore, Spencer's basis in tractor B is $55,000, for which he can claim the I.R.C. §179 expense deduction and depreciate the balance. Spencer can deduct his interest payments. He cannot claim any lease payment deductions.

RECAPTURE OF I.R.C. §179 DEDUCTIONS

An I.R.C. §179 recapture is triggered when the business use of property placed in service in an earlier year is reduced to 50% or less during the recapture period. The recapture period of the expense election is the entire recovery period of the qualifying §179 property [I.R.C. §179(d)(10)].

The recapture amount (reported on Form 4797) equals the §179 expense deduction taken minus the MACRS depreciation amount that would have been allowed on the expense amount from the time the property was placed in service up to and including the year of recapture [Treas. Reg. §1.179-1(e)(1)].

LISTED PROPERTY

If an I.R.C. §179 deduction is claimed on listed property, and the business use of the property later falls to 50% or less, the I.R.C. §179 recapture is included with the recapture of the excess depreciation [I.R.C. §280F(d)]. The I.R.C. §280F(b)(2) recapture rule requires the taxpayer to report as income the difference between:

1. The depreciation and I.R.C. §179 deduction that has been claimed, and
2. The depreciation that would have been allowed using the alternative MACRS depreciation rules.

Listed property is any of the following:

1. Any passenger automobile.
2. Any other property used for transportation.
3. Any property of a type generally used for entertainment, recreation, or amusement (including photographic, phonographic, communication, and video recording equipment).
4. Any computer and related peripheral equipment, unless it is used only at a regular business establishment and is owned or leased by the person operating the establishment. A regular business establishment includes a portion of a dwelling unit if and only if that portion is used both regularly and exclusively for business.
5. Any cellular telephone (or similar telecommunication equipment) placed in service or leased in a tax year beginning after 1989.

Example 10. Stacy Edwards paid $5,000 for a computer in 1996. She used the computer 80% in her business and 20% for personal use. Therefore, her basis in the portion used for business was $4,000. She used the computer in a room of her home that was not used exclusively for the business. She claimed a $3,000 I.R.C. §179 deduction for the computer on her 1996 income tax return. She depreciated the remaining $1,000 business basis using MACRS. She deducted the following depreciation:

Year	Depreciation Rate	Depreciation Basis	Depreciation Amt.
1996	15.00%	$1,000	$150
1997	25.50%	1,000	255
1998	17.85%	1,000	179

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Year	Depreciation Rate	Depreciation Basis	Depreciation Amt.
			$584

The total depreciation deducted through 1998 is $3,584.

In 1999 Stacy used the computer only 40% for business. Therefore, she must recapture the I.R.C. §179 deduction and depreciation claimed to the extent they exceed the depreciation that is allowed under alternative MACRS. The recapture is calculated as follows:

Alternative MACRS Depreciation Allowable (Straight-Line Method)

Year	Depreciation Rate	Depreciation Basis	Depreciation Amt.
1996	10.00%	$4,000	$400
1997	20.00%	4,000	800
1998	20.00%	4,000	800
			$2,000

Total taken	$3,584
Total allowable	(2,000)
Excess depreciation recapture	$1,584

Stacy reports the recapture on Form 4797. She also reports the $1,584 recapture amount on her 1999 Schedule C. The $3,584 reduced her self-employment income in 1995–1997, but the $1,584 recapture amount in 1999 is subject to self-employment tax.

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Form 4797 (1999) *Stacy Edwards (Example 10)* *111 22 1234* Page 2

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** (See instructions.)

			(a) Section 179	(b) Section 280F(b)(2)
33	Section 179 expense deduction or depreciation allowable in prior years	33		*3,584*
34	Recomputed depreciation. See instructions	34		*2,000*
35	Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		*1,584*

Practitioner Note. Stacy's depreciation for 1999 is zero. The $5,000 cost × 40% business use gives a $2,000 business basis. When the $2,000 of depreciation claimed in prior years is subtracted, there is no remaining business basis to be depreciated.

PROPERTY OTHER THAN LISTED PROPERTY

If the business use of property other than listed property falls to 50% or below, the taxpayer must report as ordinary income the difference between the I.R.C. §179 expense claimed and the depreciation that would have been allowed on that amount had it not been expensed.

Example 11. In 1997 Jerry Zander bought a livestock trailer that cost $10,000. In 1997 and 1998 he used the trailer 100% for hauling cattle for his farm business. He claimed $2,000 of his $10,000 business basis as an I.R.C. §179 deduction in 1997 and depreciated the remaining $8,000 business basis using 150% declining balance.

In 1999 Jerry reduced his business use of the trailer to 40% and used it 60% for his hobby, horses. That reduction in business use requires Jerry to report his excess I.R.C. §179 deduction as other income

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on line 10 of his 1999 Schedule F. The amount of the excess I.R.C. §179 deduction is calculated as follows:

Year	Depreciation Rate	Depreciation Basis	Allowable Depreciation Amt.	
1997	10.71%	$2,000	$214.20	
1998	19.13%	2,000	382.60	
1999	15.03%	2,000	120.24	($300.60 × 40%)
Total allowable			$717.04	

The excess recapture amount is $1,282.96 ($2,000 – $717.04 = $1,282.96).

Jerry reports the recapture amount on Form 4797. He also reports $1,282.96 as other income on his 1999 Schedule F and adds that amount to the basis of the trailer at the beginning of 2000.

Form 4797 (1999) *Jerry Zander (Example 11)* *123 45 6799* Page 2

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** (See instructions.)

			(a) Section 179	(b) Section 280F(b)(2)
33	Section 179 expense deduction or depreciation allowable in prior years	33	*2,000*	
34	Recomputed depreciation. See instructions	34	*717*	
35	Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35	*1,283*	

SECTION 197 INTANGIBLES

Prior to August 10, 1993, goodwill with no basis was reported on Schedule D. The Revenue Reconciliation Act of 1993 implemented a new Code section 197, which now defines most intangible assets and authorizes the amortization of the assets. Goodwill is now classified as §197 property and will be amortizable by the buyer. The general interpretation is that the new §197 rules do not alter the tax character of gain or loss realized by sellers of business intangibles that were acquired (or developed) prior to the §197 effective dates.

Example 12. There are two partners in the ABC CPA firm, Mr. Smith and Mr. Jones. In August 1990, Mr. Jones retired. Mr. Williams bought Mr. Jones's share of the firm for $50,000, all of which was for goodwill. In May 1998, Mr. Williams bought out Mr. Smith for $200,000, all of which was for goodwill. Because of health, on December 2, 1999, Mr. Williams sold the practice to an outside party for $350,000. Amortization was taken as follows:

Year	Month Purchased	Property	Depr. / Amort. Taken
1990	August	Goodwill	0
1998	May	Goodwill	Amort: $21,111 ($200,000/180 months × 19 months = $21,111)

Mr. Williams shows the sale on Form 4797 as illustrated below.

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Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

► **Attach to your tax return.** ► **See separate instructions.**

OMB No. 1545-0184

1999

Attachment Sequence No. **27**

Name(s) shown on return

Mr. Williams (Example 12)

Identifying number ***123 45 6789***

Proof as of 5/24/1999

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 . . . . . **1**

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft—Property Held More Than 1 Year

	(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2							

3	Gain, if any, from Form 4684, line 39	**3**	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	**4**	
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	**5**	
6	Gain, if any, from line 32, from other than casualty or theft	**6**	***100,000***
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	**7**	***100,000***
	Partnerships—Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below.		
	S corporations—Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax.		
	All others—If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.		
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	**8**	
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line(s) as follows (see instructions):	**9**	
	S corporations—Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below.		
	All others—If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.		

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11	Loss, if any, from line 7	**11**	( )
12	Gain, if any, from line 7 or amount from line 8, if applicable	**12**	
13	Gain, if any, from line 31	**13**	***21,110***
14	Net gain or (loss) from Form 4684, lines 31 and 38a	**14**	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	**15**	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	**16**	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	**17**	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	**18**	***21,110***
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.		
b	For individual returns:		
(1)	If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	**18b(1)**	
(2)	Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	**18b(2)**	***21,110***

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Part III **Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255**

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A *sold firm*	*various*	*12/02/98*
B		
C		
D		

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20 Gross sales price (**Note:** *See line 1 before completing.*)	20	*350,000*			
21 Cost or other basis plus expense of sale	21	*250,000*			
22 Depreciation (or depletion) allowed or allowable	22	*21,110*			
23 Adjusted basis. Subtract line 22 from line 21	23	*228,890*			
24 Total gain. Subtract line 23 from line 20	24	*121,110*			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	*21,110*			
b Enter the **smaller** of line 24 or 25a	25b	*21,110*			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975 (see instructions)	26a				
b Applicable percentage multiplied by the **smaller** of line 24 or line 26a (see instructions)	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the **smaller** of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage (see instructions)	27b				
c Enter the **smaller** of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs (see instructions)	28a				
b Enter the **smaller** of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126 (see instructions)	29a				
b Enter the **smaller** of line 24 or 29a (see instructions)	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	*121,110*
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	*21,110*
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	*100,000*

Part IV **Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less** (See instructions.)

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		

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