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Sales and Other Dispositions of Assets

For use in preparing
2005 Returns



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What's New

Extended replacement period for involuntarily converted property located in the Hurricane Katrina disaster area. The replacement period for property in the Hurricane Katrina disaster area that was involuntarily converted after August 24, 2005, has been extended from 2 years to 5 years. For details, see *Involuntary Conversions* in chapter 1. Also, see the Instructions for Form 4684, *Casualties and Thefts*.

Extended deadlines for certain like-kind exchange transactions in Presidentially declared disaster areas. Certain deadlines are extended to section 1031 like-kind exchange transactions that are affected by a Presidentially declared disaster. Acts extended include the 45-day identification period, the 180-day exchange period, the 5-business day period to enter into a qualified exchange accommodation (QEAA). For details about like-kind exchanges, see *Nontaxable Exchanges* and, for information about extended deadlines, see Revenue Procedure 2005-27 on page 1050 of Internal Revenue Bulletin 2005-20 at www.irs.gov/pub/irs-irb/irb05-20.pdf.

Important Reminders

Additional special depreciation allowances. The 30% and 50% special depreciation allowances will not apply to most property placed in service after 2004. However, the special depreciation allowances are subject to depreciation recapture. See *Depreciation Recapture* in chapter 3.

Sale of DC Zone assets. If you sold or exchanged a District of Columbia Enterprise Zone (DC Zone) asset that you held for more than 5 years, you may be able to exclude the “qualified capital gain”. For more information, see *Exclusion of Gain From Sale of DC Zone Assets* at the end of chapter 1.

Dispositions of U.S. real property interests by foreign persons. If you are a foreign person or firm and you sell or otherwise dispose of a U.S. real property interest, the buyer (or other transferee) may have to withhold income tax on the amount you receive for the property (including cash, the fair market value of other property, and any assumed liability). Corporations, partnerships, trusts, and estates also may have to withhold on certain U.S. real property interests they distribute to you. You must report these dispositions and distributions and any income tax withheld on your U.S. income tax return.

For more information on dispositions of U.S. real property interests, see Publication 519, U.S. Tax Guide for Aliens.

Foreign source income. If you are a U.S. citizen with income from dispositions of property outside the United States (foreign income), you must report all such income on your tax return unless it is exempt from U.S. law. This is true whether you reside inside or outside the United States and whether or not you receive a Form 1099 from the foreign payor.

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling 1-800-THE-LOST (1-800-843-5678) if you recognize a child.

Introduction

This publication explains the tax rules that apply when you dispose of property. It discusses the following topics.

- How to figure a gain or loss.
- Whether your gain or loss is ordinary or capital.
- How to treat your gain or loss when you dispose of business property.
- How to report a gain or loss.

This publication also explains whether your gain is taxable or your loss is deductible.

This publication does not discuss certain transactions covered in other IRS publications. These include the following.

- Most transactions involving stocks, bonds, options, forward and futures contracts, and similar investments, discussed in chapter 4 of Publication 550, *Investment Income and Expenses*.
- Sale of your main home, discussed in Publication 523, *Selling Your Home*.
- Installment sales, discussed in Publication 537, *Installment Sales*.
- Transfers of property at death, discussed in Publication 559, *Survivors, Executors, and Administrators*.

Disposing of property. You dispose of property when any of the following occurs.

- You sell property.
- You exchange property for other property.
- Your property is condemned or disposed of under threat of condemnation.
- Your property is repossessed.
- You abandon property.
- You give property away.

Forms to file. When you dispose of property, you usually will have to file one or more of the following forms.

- Schedule D (Form 1040), *Capital Gains and Losses*.
- Form 4797, *Sales of Business Property*.
- Form 8824, *Like-Kind Exchanges*.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

You can write to us at the following address.

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We respond to many letters by telephone. Therefore, it would be helpful if you would include your daytime phone number, including the area code, in your correspondence.

You can email us at taxforms@irs.gov. (The asterisk must be included in the address.) Please put “Publications Comment” on the subject line. Although we cannot respond individually to each email, we do appreciate your feedback and will consider your comments as we revise our tax products.

1.

Gain or Loss

Topics

This chapter discusses:

- Sales and exchanges
- Abandonments
- Foreclosures and repossessions
- Involuntary conversions
- Nontaxable exchanges
- Transfers to spouse
- Rollovers and exclusions for certain capital gains

Useful Items

You may want to see:

Publication

- 523** *Selling Your Home*
- 537** *Installment Sales*
- 547** *Casualties, Disasters, and Thefts*
- 550** *Investment Income and Expenses*
- 551** *Basis of Assets*
- 908** *Bankruptcy Tax Guide*
- 954** *Tax Incentives for Distressed Communities*

Form (and Instructions)

- Schedule D (Form 1040)** *Capital Gains and Losses*
- 1040** *U.S. Individual Income Tax Return*
- 1040X** *Amended U.S. Individual Income Tax Return*
- 1099-A** *Acquisition or Abandonment of Secured Property*
- 1099-C** *Cancellation of Debt*
- 4797** *Sales of Business Property*
- 8824** *Like-Kind Exchanges*

See chapter 5 for information about getting publications and forms.

Sales and Exchanges

The following discussions describe the kinds of transactions that are treated as sales or exchanges and explain how to figure gain or loss. A sale is a transfer of property for money or a mortgage, note, or other promise to pay money. An exchange is a transfer of property for other property or services.

Sale or lease. Some agreements that seem to be leases may really be conditional sales contracts. The intention of the parties to the agree-

ment can help you distinguish between a sale and a lease.

There is no test or group of tests to prove what the parties intended when they made the agreement. You should consider each agreement based on its own facts and circumstances. For more information on leases, see chapter 4 in Publication 535, Business Expenses.

Cancellation of a lease. Payments received by a tenant for the cancellation of a lease are treated as an amount realized from the sale of property. Payments received by a landlord (lessor) for the cancellation of a lease are essentially a substitute for rental payments and are taxed as ordinary income in the year in which they are received.

Copyright. Payments you receive for granting the exclusive use of (or right to exploit) a copyright throughout its life in a particular medium are treated as received from the sale of property. It does not matter if the payments are a fixed amount or a percentage of receipts from the sale, performance, exhibition, or publication of the copyrighted work, or an amount based on the number of copies sold, performances given, or exhibitions made. Nor does it matter if the payments are made over the same period as that covering the grantee's use of the copyrighted work.

If the copyright was used in your trade or business and you held it longer than a year, the gain or loss may be a section 1231 gain or loss. For more information, see *Section 1231 Gains and Losses* in chapter 3.

Easement. The amount received for granting an easement is subtracted from the basis of the property. If only a specific part of the entire tract of property is affected by the easement, only the basis of that part is reduced by the amount received. If it is impossible or impractical to separate the basis of the part of the property on which the easement is granted, the basis of the whole property is reduced by the amount received.

Any amount received that is more than the basis to be reduced is a taxable gain. The transaction is reported as a sale of property.

If you transfer a perpetual easement for consideration and do not keep any beneficial interest in the part of the property affected by the easement, the transaction will be treated as a sale of property. However, if you make a qualified conservation contribution of a restriction or easement granted in perpetuity, it is treated as a charitable contribution and not a sale or exchange, even though you keep a beneficial interest in the property affected by the easement.

If you grant an easement on your property (for example, a right-of-way over it) under condemnation or threat of condemnation, you are considered to have made a forced sale, even though you keep the legal title. Although you figure gain or loss on the easement in the same way as a sale of property, the gain or loss is treated as a gain or loss from a condemnation. See *Gain or Loss From Condemnations*, later.

Property transferred to satisfy debt. A transfer of property to satisfy a debt is an exchange.

Note's maturity date extended. The extension of a note's maturity date is not treated as an exchange of an outstanding note for a new and different note. Also, it is not considered a closed

and completed transaction that would result in a gain or loss. However, an extension will be treated as a taxable exchange of the outstanding note for a new and materially different note if the changes in the terms of the note are significant. Each case must be determined by its own facts.

Transfer on death. The transfer of property to an executor or administrator on the death of an individual is not a sale or exchange.

Bankruptcy. Generally, a transfer of property from a debtor to a bankruptcy estate is not treated as a sale or exchange. For more information, see *The Bankruptcy Estate* in Publication 908.

Gain or Loss From Sales and Exchanges

Gain or loss is usually realized when property is sold or exchanged. A gain is the amount you realize from a sale or exchange of property that is more than its adjusted basis. A loss is the adjusted basis of the property that is more than the amount you realize.

Table 1-1. How To Figure Whether You Have a Gain or Loss

| IF your... | THEN you have a... |
|--------------------------------------------------|--------------------|
| Adjusted basis is more than the amount realized, | Loss. |
| Amount realized is more than the adjusted basis, | Gain. |

Basis. You must know the basis of your property to determine whether you have a gain or loss from its sale or other disposition. The basis of property you buy is usually its cost. However, if you acquired the property by gift, inheritance, or in some way other than buying it, you must use a basis other than its cost. See *Basis Other Than Cost* in Publication 551.

Adjusted basis. The adjusted basis of property is your original cost or other basis plus certain additions and minus certain deductions, such as depreciation and casualty losses. See *Adjusted Basis* in Publication 551. In determining gain or loss, the costs of transferring property to a new owner, such as selling expenses, are added to the adjusted basis of the property.

Amount realized. The amount you realize from a sale or exchange is the total of all money you receive plus the fair market value of all property or services you receive. The amount you realize also includes any of your liabilities that were assumed by the buyer and any liabilities to which the property you transferred is subject, such as real estate taxes or a mortgage.

If the liabilities relate to an exchange of multiple properties, see *Treatment of liabilities under Multiple Property Exchanges*, later.

Fair market value. Fair market value (FMV) is the price at which the property would change hands between a buyer and a seller when both have reasonable knowledge of all the necessary facts and neither has to buy or sell. If parties with adverse interests place a value on property in an arm's-length transaction, that is strong evidence of FMV. If there is a stated price for services, this

price is treated as the FMV unless there is evidence to the contrary.

Example. You used a building in your business that cost you \$70,000. You made certain permanent improvements at a cost of \$20,000 and deducted depreciation totaling \$10,000. You sold the building for \$100,000 plus property having an FMV of \$20,000. The buyer assumed your real estate taxes of \$3,000 and a mortgage of \$17,000 on the building. The selling expenses were \$4,000. Your gain on the sale is figured as follows.

| | | | |
|------------------------------------|-------|-----------|-----------|
| Amount realized: | | | |
| Cash | ..... | \$100,000 | |
| FMV of property received | ..... | 20,000 | |
| Real estate taxes assumed by buyer | .. | 3,000 | |
| Mortgage assumed by buyer | ..... | 17,000 | \$140,000 |
| Adjusted basis: | | | |
| Cost of building | .... | \$70,000 | |
| Improvements | .... | 20,000 | |
| Total | ..... | \$90,000 | |
| Minus: Depreciation | ..... | 10,000 | |
| Adjusted basis | .... | \$80,000 | |
| Plus: Selling expenses | ..... | 4,000 | \$84,000 |
| Gain on sale | ..... |  | \$56,000 |

Amount recognized. Your gain or loss realized from a sale or exchange of property is usually a recognized gain or loss for tax purposes. Recognized gains must be included in gross income. Recognized losses are deductible from gross income. However, your gain or loss realized from certain exchanges of property is not recognized for tax purposes. See *Nontaxable Exchanges*, later. Also, a loss from the sale or other disposition of property held for personal use is not deductible, except in the case of a casualty or theft.

Interest in property. The amount you realize from the disposition of a life interest in property, an interest in property for a set number of years, or an income interest in a trust is a recognized gain under certain circumstances. If you received the interest as a gift, inheritance, or in a transfer from a spouse or former spouse incident to a divorce, the amount realized is a recognized gain. Your basis in the property is disregarded. This rule does not apply if all interests in the property are disposed of at the same time.

Example 1. Your father dies and leaves his farm to you for life with a remainder interest to your younger brother. You decide to sell your life interest in the farm. The entire amount you receive is a recognized gain. Your basis in the farm is disregarded.

Example 2. The facts are the same as in Example 1, except that your brother joins you in selling the farm. The entire interest in the property is sold, so your basis in the farm is not disregarded. Your gain or loss is the difference between your share of the sales price and your adjusted basis in the farm.

Canceling a sale of real property. If you sell real property under a sales contract that allows the buyer to return the property for a full refund and the buyer does so, you may not have to recognize gain or loss on the sale. If the buyer returns the property in the year of sale, no gain

or loss is recognized. This cancellation of the sale in the same year it occurred places both you and the buyer in the same positions you were in before the sale. If the buyer returns the property in a later tax year, however, you must recognize gain (or loss, if allowed) in the year of the sale. When the property is returned in a later year, you acquire a new basis in the property. That basis is equal to the amount you pay to the buyer.

Bargain Sale

If you sell or exchange property for less than fair market value with the intent of making a gift, the transaction is partly a sale or exchange and partly a gift. You have a gain if the amount realized is more than your adjusted basis in the property. However, you do not have a loss if the amount realized is less than the adjusted basis of the property.

Bargain sales to charity. A bargain sale of property to a charitable organization is partly a sale or exchange and partly a charitable contribution. If a charitable deduction for the contribution is allowable, you must allocate your adjusted basis in the property between the part sold and the part contributed based on the fair market value of each. The adjusted basis of the part sold is figured as follows.

| | | | |
|-----------------------------------|---|--------------------------------------------------|--|
| Adjusted basis of entire property | X | Amount realized (fair market value of part sold) | |
| | | Fair market value of entire property | |

Based on this allocation rule, you will have a gain even if the amount realized is not more than your adjusted basis in the property. This allocation rule does not apply if a charitable contribution deduction is not allowable.

See Publication 526, Charitable Contributions, for information on figuring your charitable contribution.

Example. You sold property with a fair market value of \$10,000 to a charitable organization for \$2,000 and are allowed a deduction for your contribution. Your adjusted basis in the property is \$4,000. Your gain on the sale is \$1,200, figured as follows.

| | |
|---------------------------------------------------------------------|----------------|
| Sales price | \$2,000 |
| Minus: Adjusted basis of part sold (\$4,000 × (\$2,000 ÷ \$10,000)) | 800 |
| Gain on the sale | <u>\$1,200</u> |

Property Used Partly for Business or Rental

If you sell or exchange property you used partly for business or rental purposes and partly for personal purposes, you must figure the gain or loss on the sale or exchange as though you had sold two separate pieces of property. You must allocate the selling price, selling expenses, and the basis of the property between the business or rental part and the personal part. You must subtract depreciation you took or could have taken from the basis of the business or rental part.

Gain or loss on the business or rental part of the property may be a capital gain or loss or an ordinary gain or loss, as discussed in chapter 3

under Section 1231 Gains and Losses. Any gain on the personal part of the property is a capital gain. You cannot deduct a loss on the personal part.

Example. You sold a condominium for \$57,000. You had bought the property 9 years earlier in January for \$30,000. You used two-thirds of it as your home and rented out the other third. You claimed depreciation of \$3,272 for the rented part during the time you owned the property. You made no improvements to the property. Your selling expenses for the condominium were \$3,600. You figure your gain or loss as follows.

| | Rental (1/3) | Personal (2/3) |
|-------------------------------------------|-----------------|-----------------|
| 1) Selling price | \$19,000 | \$38,000 |
| 2) Minus: Selling expenses | 1,200 | 2,400 |
| 3) Amount realized (adjusted sales price) | 17,800 | 35,600 |
| 4) Basis | 10,000 | 20,000 |
| 5) Minus: Depreciation | 3,272 | |
| 6) Adjusted basis | 6,728 | 20,000 |
| 7) Gain (line 3 – line 6) | <u>\$11,072</u> | <u>\$15,600</u> |

Property Changed to Business or Rental Use

You cannot deduct a loss on the sale of property you acquired for use as your home and used as your home until the time of sale.

You can deduct a loss on the sale of property you acquired for use as your home but changed to business or rental property and used as business or rental property at the time of sale. However, if the adjusted basis of the property at the time of the change was more than its fair market value, the loss you can deduct is limited.

Figure the loss you can deduct as follows.

1. Use the lesser of the property's adjusted basis or fair market value at the time of the change.
2. Add to (1) the cost of any improvements and other increases to basis since the change.
3. Subtract from (2) depreciation and any other decreases to basis since the change.
4. Subtract the amount you realized on the sale from the result in (3). If the amount you realized is more than the result in (3), treat this result as zero.

The result in (4) is the loss you can deduct.

Example. You changed your main home to rental property 5 years ago. At the time of the change, the adjusted basis of your home was \$75,000 and the fair market value was \$70,000. This year, you sold the property for \$55,000. You made no improvements to the property but you have depreciation expense of \$12,620 over the 5 prior years. Although your loss on the sale is \$7,380 [(\$75,000 – \$12,620) – \$55,000], the amount you can deduct as a loss is limited to \$2,380, figured as follows.

| | |
|----------------------------------------------------------------------------------|------------|
| Lesser of adjusted basis or fair market value at time of the change | \$70,000 |
| Plus: Cost of any improvements and any other additions to basis after the change | |
| | <u>-0-</u> |

| | |
|-----------------------------------------------------------------------|---------------|
| 70,000 | |
| Minus: Depreciation and any other decreases to basis after the change | <u>12,620</u> |
| | <u>57,380</u> |

| | |
|------------------------------------------|----------------|
| Minus: Amount you realized from the sale | <u>55,000</u> |
| Deductible loss | <u>\$2,380</u> |

Gain. If you have a gain on the sale, you generally must recognize the full amount of the gain. You figure the gain by subtracting your adjusted basis from your amount realized, as described earlier.

You may be able to exclude all or part of the gain if you owned and lived in the property as your main home for at least 2 years during the 5-year period ending on the date of sale. For more information, see Publication 523.

Abandonments

The abandonment of property is a disposition of property. You abandon property when you voluntarily and permanently give up possession and use of the property with the intention of ending your ownership but without passing it on to anyone else.

Loss from abandonment of business or investment property is deductible as an ordinary loss, even if the property is a capital asset. The loss is the property's adjusted basis when abandoned. This rule also applies to leasehold improvements the lessor made for the lessee that were abandoned. However, if the property is later foreclosed on or repossessed, gain or loss is figured as discussed later. The abandonment loss is deducted in the tax year in which the loss is sustained.

You cannot deduct any loss from abandonment of your home or other property held for personal use.

Example. Ann abandoned her home that she bought for \$200,000. At the time she abandoned the house, her mortgage balance was \$185,000. She has a nondeductible loss of \$200,000 (the adjusted basis). If the bank later forecloses on the loan or repossesses the house, she will have to figure her gain or loss as discussed later under *Foreclosures and Repossessions*.

Cancellation of debt. If the abandoned property secures a debt for which you are personally liable and the debt is canceled, you will realize ordinary income equal to the canceled debt. This income is separate from any loss realized from abandonment of the property. Report income from cancellation of a debt related to a business or rental activity as business or rental income. Report income from cancellation of a nonbusiness debt as other income on Form 1040, line 21.

However, income from cancellation of debt is not taxed if any of the following conditions apply.

- The cancellation is intended as a gift.
- The debt is qualified farm debt (see chapter 3 of Publication 225, Farmer's Tax Guide).

Table 1-2. Worksheet for Foreclosures and Repossessions
(Keep for your records)



| | |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------|
| Part 1. Figure your income from cancellation of debt. (Note: <i>If you are not personally liable for the debt, you do not have income from cancellation of debt. Skip Part 1 and go to Part 2.</i>) | |
| 1. Enter the amount of debt canceled by the transfer of property | _____ |
| 2. Enter the fair market value of the transferred property | _____ |
| 3. Income from cancellation of debt.* Subtract line 2 from line 1. If less than zero, enter zero | ===== |
| Part 2. Figure your gain or loss from foreclosure or repossession. | |
| 4. Enter the smaller of line 1 or line 2. Also include any proceeds you received from the foreclosure sale. (If you are not personally liable for the debt, enter the amount of debt canceled by the transfer of property.) | _____ |
| 5. Enter the adjusted basis of the transferred property | _____ |
| 6. Gain or loss from foreclosure or repossession. Subtract line 5 from line 4 | ===== |

* The income may not be taxable. See *Cancellation of debt*.

- The debt is qualified real property business debt (see chapter 5 of Publication 334, Tax Guide for Small Business).
- You are insolvent or bankrupt (see Publication 908).

Forms 1099-A and 1099-C. If your abandoned property secures a loan and the lender knows the property has been abandoned, the lender should send you Form 1099-A showing information you need to figure your loss from the abandonment. However, if your debt is canceled and the lender must file Form 1099-C, the lender may include the information about the abandonment on that form instead of on Form 1099-A. The lender must file Form 1099-C and send you a copy if the amount of debt canceled is \$600 or more and the lender is a financial institution, credit union, federal government agency, or any organization that has a significant trade or business of lending money. For abandonments of property and debt cancellations occurring in 2005, these forms should be sent to you by January 31, 2006.

Foreclosures and Repossessions

If you do not make payments you owe on a loan secured by property, the lender may foreclose on the loan or repossess the property. The foreclosure or repossession is treated as a sale or exchange from which you may realize gain or loss. This is true even if you voluntarily return the property to the lender. You also may realize ordinary income from cancellation of debt if the loan balance is more than the fair market value of the property.

Buyer's (borrower's) gain or loss. You figure and report gain or loss from a foreclosure or repossession in the same way as gain or loss from a sale or exchange. The gain or loss is the difference between your adjusted basis in the transferred property and the amount realized. See *Gain or Loss From Sales and Exchanges*, earlier.



You can use Table 1-2 to figure your gain or loss from a foreclosure or repossession.

Amount realized on a nonrecourse debt. If you are not personally liable for repaying the debt (nonrecourse debt) secured by the transferred property, the amount you realize includes the full debt canceled by the transfer. The full canceled debt is included even if the fair market value of the property is less than the canceled debt.

Example 1. Chris bought a new car for \$15,000. He paid \$2,000 down and borrowed the remaining \$13,000 from the dealer's credit company. Chris is not personally liable for the loan (nonrecourse), but pledges the new car as security. The credit company repossessed the car because he stopped making loan payments. The balance due after taking into account the payments Chris made was \$10,000. The fair market value of the car when repossessed was \$9,000. The amount Chris realized on the repossession is \$10,000. That is the debt canceled by the repossession, even though the car's fair market value is less than \$10,000. Chris figures his gain or loss on the repossession by comparing the amount realized (\$10,000) with his adjusted basis (\$15,000). He has a \$5,000 nondeductible loss.

Example 2. Abena paid \$200,000 for her home. She paid \$15,000 down and borrowed the remaining \$185,000 from a bank. Abena is not personally liable for the loan (nonrecourse debt), but pledges the house as security. The bank foreclosed on the loan because Abena stopped making payments. When the bank foreclosed on the loan, the balance due was \$180,000, the fair market value of the house was \$170,000, and Abena's adjusted basis was \$175,000 due to a casualty loss she had deducted. The amount Abena realized on the foreclosure is \$180,000, the debt canceled by the foreclosure. She figures her gain or loss by comparing the amount realized (\$180,000) with her adjusted basis (\$175,000). She has a \$5,000 realized gain.

Amount realized on a recourse debt. If you are personally liable for the debt (recourse debt), the amount realized on the foreclosure or repossession does not include the canceled

debt that is your income from cancellation of debt. However, if the fair market value of the transferred property is less than the canceled debt, the amount realized includes the canceled debt up to the fair market value of the property. You are treated as receiving ordinary income from the canceled debt for the part of the debt that is more than the fair market value. See *Cancellation of debt*, later.

Example 1. Assume the same facts as in the previous Example 1, except Chris is personally liable for the car loan (recourse debt). In this case, the amount he realizes is \$9,000. This is the canceled debt (\$10,000) up to the car's fair market value (\$9,000). Chris figures his gain or loss on the repossession by comparing the amount realized (\$9,000) with his adjusted basis (\$15,000). He has a \$6,000 nondeductible loss. He also is treated as receiving ordinary income from cancellation of debt. That income is \$1,000 (\$10,000 - \$9,000). This is the part of the canceled debt not included in the amount realized.

Example 2. Assume the same facts as in the previous Example 2, except Abena is personally liable for the loan (recourse debt). In this case, the amount she realizes is \$170,000. This is the canceled debt (\$180,000) up to the fair market value of the house (\$170,000). Abena figures her gain or loss on the foreclosure by comparing the amount realized (\$170,000) with her adjusted basis (\$175,000). She has a \$5,000 nondeductible loss. She also is treated as receiving ordinary income from cancellation of debt. That income is \$10,000 (\$180,000 - \$170,000). This is the part of the canceled debt not included in the amount realized.

Seller's (lender's) gain or loss on repossession. If you finance a buyer's purchase of property and later acquire an interest in it through foreclosure or repossession, you may have a gain or loss on the acquisition. For more information, see *Repossession* in Publication 537.

Cancellation of debt. If property that is repossessed or foreclosed on secures a debt for which you are personally liable (recourse debt), you generally must report as ordinary income the amount by which the canceled debt is more than the fair market value of the property. This income is separate from any gain or loss realized from the foreclosure or repossession. Report the income from cancellation of a debt related to a business or rental activity as business or rental income. Report the income from cancellation of a nonbusiness debt as other income on Form 1040, line 21.



You can use Table 1-2 to figure your income from cancellation of debt.

However, income from cancellation of debt is not taxed if any of the following conditions apply.

- The cancellation is intended as a gift.
- The debt is qualified farm debt (see chapter 3 of Publication 225, Farmer's Tax Guide).
- The debt is qualified real property business debt (see chapter 5 of Publication 334, Tax Guide for Small Business).
- You are insolvent or bankrupt (see Publication 908).



Table 1-3. Worksheet for Condemnations
(Keep for your records)

| | |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------|
| Part 1. Gain from severance damages. | |
| (If you did not receive severance damages, skip Part 1 and go to Part 2.) | |
| 1. Enter severance damages received | _____ |
| 2. Enter your expenses in getting severance damages | _____ |
| 3. Subtract line 2 from line 1. If less than zero, enter -0- | _____ |
| 4. Enter any special assessment on remaining property taken out of your award | _____ |
| 5. Net severance damages. Subtract line 4 from line 3. If less than zero, enter -0- | _____ |
| 6. Enter the adjusted basis of the remaining property | _____ |
| 7. Gain from severance damages. Subtract line 6 from line 5. If less than zero, enter -0- | _____ |
| 8. Refigured adjusted basis of the remaining property. Subtract line 5 from line 6. If less than zero, enter -0- | _____ |
| Part 2. Gain or loss from condemnation award. | |
| 9. Enter the condemnation award received | _____ |
| 10. Enter your expenses in getting the condemnation award | _____ |
| 11. If you completed Part 1, and line 4 is more than line 3, subtract line 3 from line 4. Otherwise, enter -0- | _____ |
| 12. Add lines 10 and 11 | _____ |
| 13. Net condemnation award. Subtract line 12 from line 9 | _____ |
| 14. Enter the adjusted basis of the condemned property | _____ |
| 15. Gain from condemnation award. If line 14 is more than line 13, enter -0-. Otherwise, subtract line 14 from line 13 and skip line 16 | _____ |
| 16. Loss from condemnation award. Subtract line 13 from line 14 | _____ |
| <i>(Note: You cannot deduct the amount on line 16 if the condemned property was held for personal use.)</i> | |
| Part 3. Postponed gain from condemnation. | |
| (Complete only if line 7 or line 15 is more than zero and you bought qualifying replacement property or made expenditures to restore the usefulness of your remaining property.) | |
| 17. If you completed Part 1, and line 7 is more than zero, enter the amount from line 5. Otherwise, enter -0- | _____ |
| 18. If line 15 is more than zero, enter the amount from line 13. Otherwise, enter -0- | _____ |
| 19. Add lines 17 and 18* | _____ |
| 20. Enter the total cost of replacement property and any expenses to restore the usefulness of your remaining property | _____ |
| 21. Subtract line 20 from line 19. If less than zero, enter -0- | _____ |
| 22. If you completed Part 1, add lines 7 and 15. Otherwise, enter the amount from line 15 | _____ |
| 23. Recognized gain. Enter the smaller of line 21 or line 22. | _____ |
| 24. Postponed gain. Subtract line 23 from line 22. If less than zero, enter -0- | _____ |

*If the condemned property was your main home, subtract from this total the gain you excluded from your income and enter the result.

Forms 1099-A and 1099-C. A lender who acquires an interest in your property in a foreclosure or repossession should send you Form 1099-A showing the information you need to figure your gain or loss. However, if the lender also cancels part of your debt and must file Form 1099-C, the lender may include the information about the foreclosure or repossession on that form instead of on Form 1099-A. The lender must file Form 1099-C and send you a copy if the amount of debt canceled is \$600 or more and the lender is a financial institution, credit union, federal government agency, or any organization that has a significant trade or business of lending money. For foreclosures or repossessions occurring in 2005, these forms should be sent to you by January 31, 2006.

Involuntary Conversions

An involuntary conversion occurs when your property is destroyed, stolen, condemned, or disposed of under the threat of condemnation and you receive other property or money in payment, such as insurance or a condemnation award. Involuntary conversions are also called involuntary exchanges.

Gain or loss from an involuntary conversion of your property is usually recognized for tax purposes unless the property is your main home. You report the gain or deduct the loss on your tax return for the year you realize it. (You cannot deduct a loss from an involuntary conversion of property you held for personal use unless the loss resulted from a casualty or theft.)

However, depending on the type of property you receive, you may not have to report a gain on an involuntary conversion. You do not report the gain if you receive property that is similar or related in service or use to the converted property. Your basis for the new property is the same as your basis for the converted property. This means that the gain is deferred until a taxable sale or exchange occurs.

If you receive money or property that is not similar or related in service or use to the involuntarily converted property and you buy qualifying replacement property within a certain period of time, you can choose to postpone reporting the gain.

This publication explains the treatment of a gain or loss from a condemnation or disposition under the threat of condemnation. If you have a gain or loss from the destruction or theft of property, see Publication 547.

Condemnations

A condemnation is the process by which private property is legally taken for public use without the owner's consent. The property may be taken by the federal government, a state government, a political subdivision, or a private organization that has the power to legally take it. The owner receives a condemnation award (money or property) in exchange for the property taken. A condemnation is like a forced sale, the owner being the seller and the condemning authority being the buyer.

Example. A local government authorized to acquire land for public parks informed you that it wished to acquire your property. After the local government took action to condemn your property, you went to court to keep it. But, the court decided in favor of the local government, which took your property and paid you an amount fixed by the court. This is a condemnation of private property for public use.

Threat of condemnation. A threat of condemnation exists if a representative of a government body or a public official authorized to acquire property for public use informs you that the government body or official has decided to acquire your property. You must have reasonable grounds to believe that, if you do not sell voluntarily, your property will be condemned.

The sale of your property to someone other than the condemning authority will also qualify as an involuntary conversion, provided you have reasonable grounds to believe that your property will be condemned. If the buyer of this property knows at the time of purchase that it will be condemned and sells it to the condemning authority, this sale also qualifies as an involuntary conversion.

Reports of condemnation. A threat of condemnation exists if you learn of a decision to acquire your property for public use through a report in a newspaper or other news medium, and this report is confirmed by a representative of the government body or public official involved. You must have reasonable grounds to believe that they will take necessary steps to condemn your property if you do not sell voluntarily. If you relied on oral statements made by a government representative or public official, the Internal Revenue Service may ask you to get written confirmation of the statements.

Example. Your property lies along public utility lines. The utility company has the authority to condemn your property. The company informs you that it intends to acquire your property by negotiation or condemnation. A threat of condemnation exists when you receive the notice.

Related property voluntarily sold. A voluntary sale of your property may be treated as a forced sale that qualifies as an involuntary conversion if the property had a substantial economic relationship to property of yours that was condemned. A substantial economic relationship exists if together the properties were one economic unit. You also must show that the condemned property could not reasonably or adequately be replaced. You can choose to postpone reporting the gain by buying replacement property. See *Postponement of Gain*, later.

Gain or Loss From Condemnations

If your property was condemned or disposed of under the threat of condemnation, figure your gain or loss by comparing the adjusted basis of your condemned property with your net condemnation award.

If your net condemnation award is more than the adjusted basis of the condemned property, you have a gain. You can postpone reporting gain from a condemnation if you buy replacement property. If only part of your property is condemned, you can treat the cost of restoring the remaining part to its former usefulness as the cost of replacement property. See *Postponement of Gain*, later.

If your net condemnation award is less than your adjusted basis, you have a loss. If your loss is from property you held for personal use, you cannot deduct it. You must report any deductible loss in the tax year it happened.



You can use Part 2 of Table 1-3 to figure your gain or loss from a condemnation award.

Main home condemned. If you have a gain because your main home is condemned, you generally can exclude the gain from your income as if you had sold or exchanged your home. You may be able to exclude up to \$250,000 of the

gain (up to \$500,000 if married filing jointly). For information on this exclusion, see Publication 523. If your gain is more than you can exclude but you buy replacement property, you may be able to postpone reporting the rest of the gain. See *Postponement of Gain*, later.

Condemnation award. A condemnation award is the money you are paid or the value of other property you receive for your condemned property. The award is also the amount you are paid for the sale of your property under threat of condemnation.

Payment of your debts. Amounts taken out of the award to pay your debts are considered paid to you. Amounts the government pays directly to the holder of a mortgage or lien against your property are part of your award, even if the debt attaches to the property and is not your personal liability.

Example. The state condemned your property for public use. The award was set at \$200,000. The state paid you only \$148,000 because it paid \$50,000 to your mortgage holder and \$2,000 accrued real estate taxes. You are considered to have received the entire \$200,000 as a condemnation award.

Interest on award. If the condemning authority pays you interest for its delay in paying your award, it is not part of the condemnation award. You must report the interest separately as ordinary income.

Payments to relocate. Payments you receive to relocate and replace housing because you have been displaced from your home, business, or farm as a result of federal or federally assisted programs are not part of the condemnation award. Do not include them in your income. Replacement housing payments used to buy new property are included in the property's basis as part of your cost.

Net condemnation award. A net condemnation award is the total award you received, or are considered to have received, for the condemned property minus your expenses of obtaining the award. If only a part of your property was condemned, you also must reduce the award by any special assessment levied against the part of the property you retain. This is discussed later under *Special assessment taken out of award*.

Severance damages. Severance damages are not part of the award paid for the property condemned. They are paid to you if part of your property is condemned and the value of the part you keep is decreased because of the condemnation.

For example, you may receive severance damages if your property is subject to flooding because you sell flowage easement rights (the condemned property) under threat of condemnation. Severance damages also may be given to you if, because part of your property is condemned for a highway, you must replace fences, dig new wells or ditches, or plant trees to restore your remaining property to the same usefulness it had before the condemnation.

The contracting parties should agree on the specific amount of severance damages in writing. If this is not done, all proceeds from the condemning authority are considered awarded for your condemned property.

You cannot make a completely new allocation of the total award after the transaction is completed. However, you can show how much of the award both parties intended for severance damages. The severance damages part of the award is determined from all the facts and circumstances.

Example. You sold part of your property to the state under threat of condemnation. The contract you and the condemning authority signed showed only the total purchase price. It did not specify a fixed sum for severance damages. However, at settlement, the condemning authority gave you closing papers showing clearly the part of the purchase price that was for severance damages. You may treat this part as severance damages.

Treatment of severance damages. Your net severance damages are treated as the amount realized from an involuntary conversion of the remaining part of your property. Use them to reduce the basis of the remaining property. If the amount of severance damages is based on damage to a specific part of the property you kept, reduce the basis of only that part by the net severance damages.

If your net severance damages are more than the basis of your retained property, you have a gain. You may be able to postpone reporting the gain. See *Postponement of Gain*, later.



You can use Part 1 of Table 1-3 to figure any gain from severance damages and to refigure the adjusted basis of the remaining part of your property.

Net severance damages. To figure your net severance damages, you first must reduce your severance damages by your expenses in obtaining the damages. You then reduce them by any special assessment (described later) levied against the remaining part of the property and taken out of the award by the condemning authority. The balance is your net severance damages.

Expenses of obtaining a condemnation award and severance damages. Subtract the expenses of obtaining a condemnation award, such as legal, engineering, and appraisal fees, from the total award. Also, subtract the expenses of obtaining severance damages, that may include similar expenses, from the severance damages paid to you. If you cannot determine which part of your expenses is for each part of the condemnation proceeds, you must make a proportionate allocation.

Example. You receive a condemnation award and severance damages. One-fourth of the total was designated as severance damages in your agreement with the condemning authority. You had legal expenses for the entire condemnation proceeding. You cannot determine how much of your legal expenses is for each part of the condemnation proceeds. You must allocate one-fourth of your legal expenses to the severance damages and the other three-fourths to the condemnation award.

Special assessment taken out of award. When only part of your property is condemned, a special assessment levied against the remaining property may be taken out of your condemnation award. An assessment may be levied if

the remaining part of your property benefited by the improvement resulting from the condemnation. Examples of improvements that may cause a special assessment are widening a street and installing a sewer.

To figure your net condemnation award, you generally reduce the award by the assessment taken out of the award.

Example. To widen the street in front of your home, the city condemned a 25-foot deep strip of your land. You were awarded \$5,000 for this and spent \$300 to get the award. Before paying the award, the city levied a special assessment of \$700 for the street improvement against your remaining property. The city then paid you only \$4,300. Your net award is \$4,000 (\$5,000 total award minus \$300 expenses in obtaining the award and \$700 for the special assessment taken out).

If the \$700 special assessment were not taken out of the award and you were paid \$5,000, your net award would be \$4,700 (\$5,000 – \$300). The net award would not change, even if you later paid the assessment from the amount you received.

Severance damages received. If severance damages are included in the condemnation proceeds, the special assessment taken out is first used to reduce the severance damages. Any balance of the special assessment is used to reduce the condemnation award.

Example. You were awarded \$4,000 for the condemnation of your property and \$1,000 for severance damages. You spent \$300 to obtain the severance damages. A special assessment of \$800 was taken out of the award. The \$1,000 severance damages are reduced to zero by first subtracting the \$300 expenses and then \$700 of the special assessment. Your \$4,000 condemnation award is reduced by the \$100 balance of the special assessment, leaving a \$3,900 net condemnation award.

Part business or rental. If you used part of your condemned property as your home and part as business or rental property, treat each part as a separate property. Figure your gain or loss separately because gain or loss on each part may be treated differently.

Some examples of this type of property are a building in which you live and operate a grocery, and a building in which you live on the first floor and rent out the second floor.

Example. You sold your building for \$24,000 under threat of condemnation to a public utility company that had the authority to condemn. You rented half the building and lived in the other half. You paid \$25,000 for the building and spent an additional \$1,000 for a new roof. You claimed allowable depreciation of \$4,600 on the rental half. You spent \$200 in legal expenses to obtain the condemnation award. Figure your gain or loss as follows.

| | <u>Resi- dential Part</u> | <u>Busi- ness Part</u> |
|-------------------------------------------|-----------------------------------|--------------------------------|
| 1) Condemnation award received | \$12,000 | \$12,000 |
| 2) Minus: Legal expenses, \$200 | 100 | 100 |
| 3) Net condemnation award | \$11,900 | \$11,900 |

| | | | |
|--------------------------------------|------------------|-----------------|--|
| 4) Adjusted basis: | | | |
| 1/2 of original cost, | | | |
| \$25,000 Plus: 1/2 of | | | |
| cost of roof, | \$12,500 | \$12,500 | |
| 1,000 | 500 | 500 | |
| Total | <u>\$13,000</u> | <u>\$13,000</u> | |
| 5) Minus: Depreciation . . | | 4,600 | |
| 6) Adjusted basis, | | | |
| business part | | <u>\$8,400</u> | |
| 7) (Loss) on residential | <u>(\$1,100)</u> | | |
| property | | | |
| 8) Gain on business property | | <u>\$3,500</u> | |

The loss on the residential part of the property is not deductible.

Postponement of Gain

Do not report the gain on condemned property if you receive only property that is similar or related in service or use to the condemned property. Your basis for the new property is the same as your basis for the old.

Money or unlike property received. You ordinarily must report the gain if you receive money or unlike property. You can choose to postpone reporting the gain if you buy property that is similar or related in service or use to the condemned property within the replacement period, discussed later. You also can choose to postpone reporting the gain if you buy a controlling interest (at least 80%) in a corporation owning property that is similar or related in service or use to the condemned property. See *Controlling interest in a corporation*, later.

To postpone reporting all the gain, you must buy replacement property costing at least as much as the amount realized for the condemned property. If the cost of the replacement property is less than the amount realized, you must report the gain up to the unspent part of the amount realized.

The basis of the replacement property is its cost, reduced by the postponed gain. Also, if your replacement property is stock in a corporation that owns property similar or related in service or use, the corporation generally will reduce its basis in its assets by the amount by which you reduce your basis in the stock. See *Controlling interest in a corporation*, later.

TIP You can use Part 3 of Table 1-3 to figure the gain you must report and your postponed gain.

Postponing gain on severance damages. If you received severance damages for part of your property because another part was condemned and you buy replacement property, you can choose to postpone reporting gain. See *Treatment of severance damages*, earlier. You can postpone reporting all your gain if the replacement property costs at least as much as your net severance damages plus your net condemnation award (if resulting in gain).

You also can make this choice if you spend the severance damages, together with other money you received for the condemned property (if resulting in gain), to acquire nearby property that will allow you to continue your business. If suitable nearby property is not available and you are forced to sell the remaining property and relocate in order to continue your business, see *Postponing gain on the sale of related property*, next.

If you restore the remaining property to its former usefulness, you can treat the cost of restoring it as the cost of replacement property.

Postponing gain on the sale of related property. If you sell property that is related to the condemned property and then buy replacement property, you can choose to postpone reporting gain on the sale. You must meet the requirements explained earlier under *Related property voluntarily sold*. You can postpone reporting all your gain if the replacement property costs at least as much as the amount realized from the sale plus your net condemnation award (if resulting in gain) plus your net severance damages, if any (if resulting in gain).

Buying replacement property from a related person. Certain taxpayers cannot postpone reporting gain from a condemnation if they buy the replacement property from a related person. For information on related persons, see *Non-deductible Loss under Sales and Exchanges Between Related Persons* in chapter 2.

This rule applies to the following taxpayers.

1. C corporations.
2. Partnerships in which more than 50% of the capital or profits interest is owned by C corporations.
3. All others (including individuals, partnerships (other than those in (2)), and S corporations) if the total realized gain for the tax year on all involuntarily converted properties on which there are realized gains is more than \$100,000.

For taxpayers described in (3) above, gains cannot be offset with any losses when determining whether the total gain is more than \$100,000. If the property is owned by a partnership, the \$100,000 limit applies to the partnership and each partner. If the property is owned by an S corporation, the \$100,000 limit applies to the S corporation and each shareholder.

Exception. This rule does not apply if the related person acquired the property from an unrelated person within the replacement period.

Advance payment. If you pay a contractor in advance to build your replacement property, you have not bought replacement property unless it is finished before the end of the replacement period (discussed later).

Replacement property. To postpone reporting gain, you must buy replacement property for the specific purpose of replacing your condemned property. You do not have to use the actual funds from the condemnation award to acquire the replacement property. Property you acquire by gift or inheritance does not qualify as replacement property.

Similar or related in service or use. Your replacement property must be similar or related in service or use to the property it replaces.

If the condemned property is real property you held for use in your trade or business or for investment (other than property held mainly for sale), but your replacement property is not similar or related in service or use, it will be treated as such if it is like-kind property to be held for use in a trade or business or for investment. For a discussion of like-kind property, see *Like-Kind Property* under *Like-Kind Exchanges*, later.

Owner-user. If you are an owner-user, similar or related in service or use means that replacement property must function in the same way as the property it replaces.

Example. Your home was condemned and you invested the proceeds from the condemnation in a grocery store. Your replacement property is not similar or related in service or use to the condemned property. To be similar or related in service or use, your replacement property must also be used by you as your home.

Owner-investor. If you are an owner-investor, similar or related in service or use means that any replacement property must have the same relationship of services or uses to you as the property it replaces. You decide this by determining all the following information.

- Whether the properties are of similar service to you.
- The nature of the business risks connected with the properties.
- What the properties demand of you in the way of management, service, and relations to your tenants.

Example. You owned land and a building you rented to a manufacturing company. The building was condemned. During the replacement period, you had a new building built on other land you already owned. You rented out the new building for use as a wholesale grocery warehouse. The replacement property is also rental property, so the two properties are considered similar or related in service or use if there is a similarity in all the following areas.

- Your management activities.
- The amount and kind of services you provide to your tenants.
- The nature of your business risks connected with the properties.

Leasehold replaced with fee simple property. Fee simple property you will use in your trade or business or for investment can qualify as replacement property that is similar or related in service or use to a condemned leasehold if you use it in the same business and for the identical purpose as the condemned leasehold.

A fee simple property interest generally is a property interest that entitles the owner to the entire property with unconditional power to dispose of it during his or her lifetime. A leasehold is property held under a lease, usually for a term of years.

Outdoor advertising display replaced with real property. You can choose to treat an outdoor advertising display as real property. If you make this choice and you replace the display with real property in which you hold a different kind of interest, your replacement property can qualify as like-kind property. For example, real property bought to replace a destroyed billboard and leased property on which the billboard was located qualifies as property of a like kind.

You can make this choice only if you did not claim a section 179 deduction for the display. You cannot cancel this choice unless you get the consent of the Internal Revenue Service.

An outdoor advertising display is a sign or device rigidly assembled and permanently attached to the ground, a building, or any other permanent structure used to display a commercial or other advertisement to the public.

Substituting replacement property. Once you designate certain property as replacement property on your tax return, you cannot substitute other qualified property. But, if your previously designated replacement property does not qualify, you can substitute qualified property if you acquire it within the replacement period.

Controlling interest in a corporation. You can replace property by acquiring a controlling interest in a corporation that owns property similar or related in service or use to your condemned property. You have controlling interest if you own stock having at least 80% of the combined voting power of all classes of voting stock and at least 80% of the total number of shares of all other classes of stock.

Basis adjustment to corporation's property. The basis of property held by the corporation at the time you acquired control must be reduced by your postponed gain, if any. You are not required to reduce the adjusted bases of the corporation's properties below your adjusted basis in the corporation's stock (determined after reduction by your postponed gain).

Allocate this reduction to the following classes of property in the order shown below.

1. Property that is similar or related in service or use to the condemned property.
2. Depreciable property not reduced in (1).
3. All other property.

If two or more properties fall in the same class, allocate the reduction to each property in proportion to the adjusted bases of all the properties in that class. The reduced basis of any single property cannot be less than zero.

Main home replaced. If your gain from a condemnation of your main home is more than you can exclude from your income (see *Main home condemned* under *Gain or Loss From Condemnations*, earlier), you can postpone reporting the rest of the gain by buying replacement property that is similar or related in service or use. To postpone reporting all the gain, the replacement property must cost at least as much as the amount realized from the condemnation minus the excluded gain.

You must reduce the basis of your replacement property by the postponed gain. Also, if you postpone reporting any part of your gain under these rules, you are treated as having owned and used the replacement property as your main home for the period you owned and used the condemned property as your main home.

Replacement period. To postpone reporting your gain from a condemnation, you must buy replacement property within a certain period of time. This is the replacement period.

The replacement period for a condemnation begins on the earlier of the following dates.

- The date on which you disposed of the condemned property.
- The date on which the threat of condemnation began.

The replacement period ends 2 years after the end of the first tax year in which any part of the gain on the condemnation is realized.

If real property held for use in a trade or business or for investment (not including property held primarily for sale) is condemned, the replacement period ends 3 years after the end of the first tax year in which any part of the gain on the condemnation is realized. However, this 3-year replacement period cannot be used if you replace the condemned property by acquiring control of a corporation owning property that is similar or related in service or use.

Extended replacement period for property located in the Hurricane Katrina disaster area. If property in the Hurricane Katrina disaster area is compulsorily or involuntarily converted after August 24, 2005, the replacement period ends 5 years after the end of the first tax year in which any part of the gain is realized on the involuntary conversion. This 5-year replacement period applies only if substantially all of the use of the replacement property is in the Hurricane Katrina disaster area.

New York Liberty Zone property condemned. If property in the New York Liberty Zone was condemned as a result of the September 11, 2001, terrorist attacks, the replacement period ends 5 years after the end of the first tax year in which any part of the gain on the condemnation is realized. This 5-year replacement period applies only if substantially all of the use of the replacement property is in New York City.

Determining when gain is realized. If you are a cash basis taxpayer, you realize gain when you receive payments that are more than your basis in the property. If the condemning authority makes deposits with the court, you realize gain when you withdraw (or have the right to withdraw) amounts that are more than your basis.

This applies even if the amounts received are only partial or advance payments and the full award has not yet been determined. A replacement will be too late if you wait for a final determination that does not take place in the applicable replacement period after you first realize gain.

For accrual basis taxpayers, gain (if any) accrues in the earlier year when either of the following occurs.

- All events have occurred that fix the right to the condemnation award and the amount can be determined with reasonable accuracy.
- All or part of the award is actually or constructively received.

For example, if you have an absolute right to a part of a condemnation award when it is deposited with the court, the amount deposited accrues in the year the deposit is made even though the full amount of the award is still contested.

Replacement property bought before the condemnation. If you buy your replacement property after there is a threat of condemnation but before the actual condemnation and you still hold the replacement property at the time of the condemnation, you have bought your replacement property within the replacement period. Property you acquire before there is a threat of condemnation does not qualify as replacement

