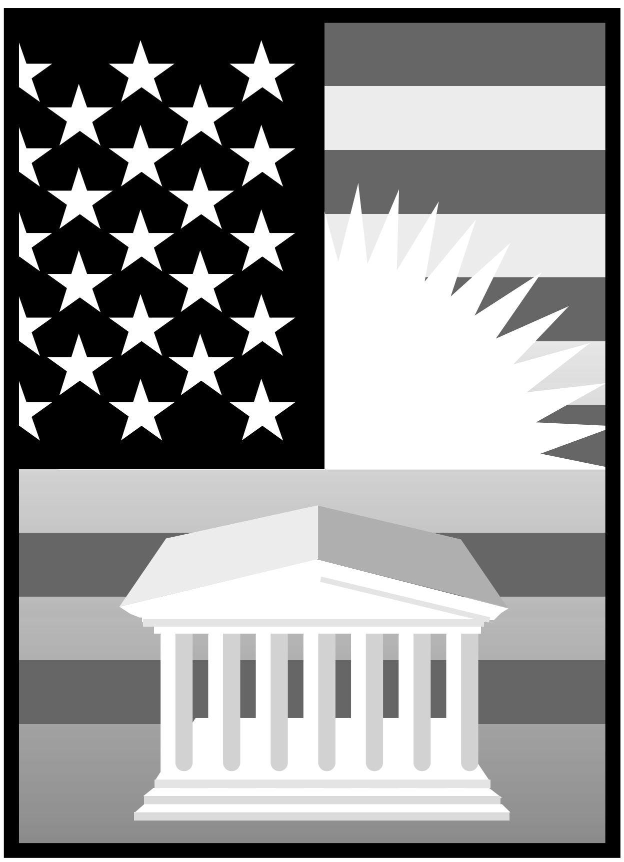
Department of the Treasury

Internal Revenue Service

Publication 551
(Rev. April 1999)
Cat. No. 15094C

Basis of Assets



Get forms and other information faster and easier by:

COMPUTER
- World Wide Web • www.irs.gov
- FTP • ftp.irs.gov

FAX
- From your FAX machine, dial • (703) 368-9694

See *How To Get More Information* in this publication.

Introduction

Basis is the amount of your investment in property for tax purposes. Use the basis of property to figure the deductions for depreciation, amortization, depletion, and casualty losses. Also use it to figure gain or loss on the sale or other disposition of property. You must keep accurate records of all items that affect the basis of property so you can make these computations.

This publication is divided into the following three sections.

- Cost Basis.
- Adjusted Basis.
- Other Basis.

The basis of property you buy is usually its cost. You may also have to capitalize (add to basis) certain other costs related to buying or producing the property.

Your original basis in property is adjusted (increased or decreased) by certain events. If you make improvements to the property, increase your basis. If you take deductions for depreciation or casualty losses, reduce your basis.

You cannot determine your basis in some assets by cost. This includes property you receive as a gift or inheritance. It also applies to property received in an involuntary conversion and certain other circumstances.

Useful Items

You may want to see:

Publication

- ☐ **463** Travel, Entertainment, Gift, and Car Expenses
- ☐ **523** Selling Your Home
- ☐ **525** Taxable and Nontaxable Income
- ☐ **527** Residential Rental Property
- ☐ **530** Tax Information for First-Time Homeowners
- ☐ **537** Installment Sales
- ☐ **544** Sales and Other Dispositions of Assets
- ☐ **550** Investment Income and Expenses
- ☐ **555** Community Property
- ☐ **559** Survivors, Executors, and Administrators
- ☐ **564** Mutual Fund Distributions
- ☐ **587** Business Use of Your Home
- ☐ **946** How To Depreciate Property

Form (and Instructions)

- ☐ **706-A** United States Additional Estate Tax Return
- ☐ **8594** Asset Acquisition Statement

See *How To Get More Information* near the end of this publication for information about getting publications and forms.

Cost Basis

Terms you may need to know (see Glossary):

Business assets
Nonbusiness assets
Real property
Unstated interest

The basis of property you buy is usually its cost. The cost is the amount you pay in cash, debt obligations, or other property. Your cost also includes amounts you pay for the following items.

- Sales tax charged on the purchase.
- Freight charges to obtain the property.
- Installation and testing charges.
- Excise taxes.
- Legal and accounting fees (when they must be capitalized).
- Revenue stamps.
- Recording fees.
- Real estate taxes (if assumed for the seller).

In addition, the basis of real property and business assets may include other items.

Loans with low or no interest. If you buy business or investment property on any time-payment plan that charges little or no interest, the basis of your property is your stated purchase price, less the amount considered to be unstated interest. You generally have unstated interest if your interest rate is less than the applicable federal rate. See the discussion of unstated interest in Publication 537.

Purchase of a business. When you purchase a trade or business, you generally purchase all assets used in the business operations, such as land, buildings, and machinery. You must spread the price among the various assets including any section 197 intangibles, such as goodwill. See *Allocating the Basis,* later.

Stocks and Bonds

The basis of stocks or bonds you buy is the purchase price plus any costs of purchase such as any commissions and recording or transfer fees.

If you acquired stock through an automatic investment program, dividend reinvestment plan, stock dividend, or by exercising stock rights, see *Stocks and Bonds* in chapter 4 of Publication 550 for information on basis.

Identifying stock or bonds sold. If you can adequately identify the shares of stock or the bonds you sold, their basis is the cost or other basis of the particular shares of stock or bonds. If you buy and sell securities at various times in varying quantities and you cannot adequately identify the shares you sell, the basis of the securities you sell is the basis of the securities you acquired first.

Mutual fund shares. If you sell mutual fund shares that you acquired at different times and prices, you may choose to use an average basis. For more information, see *Average Basis* in Publication 564.

Real Property

If you buy real property, certain fees and other expenses you pay are part of your basis in the property.

Real estate taxes. If you pay real estate taxes that the seller owed on real property you bought, and the seller did not reimburse you, treat those taxes as part of your basis. You cannot deduct them as taxes.

If you reimburse the seller for taxes the seller paid for you, you can usually deduct that amount. Do not include that amount in the basis of the property. If you did not reimburse the seller, you must reduce your basis by the amount of those taxes.

Settlement costs. You can include in the basis of property you purchase the settlement fees and closing costs that are for buying the property. You cannot include fees and costs for getting a loan on the property. (A fee is for buying property if you would have had to pay it even if you bought the property for cash.)

The following are some of the settlement fees or closing costs that you can include in the basis of your property.

- Abstract fees (abstract of title fees).
- Charges for installing utility services.
- Legal fees (including title search and preparation of the sales contract and deed).
- Recording fees.
- Surveys.
- Transfer taxes.
- Title insurance.
- Any amounts the seller owes that you agree to pay, such as back taxes or interest, recording or mortgage fees, charges for improvements or repairs, and sales commissions.

Settlement costs ***do not include*** amounts placed in escrow for the future payment of items such as taxes and insurance.

The following are some of the settlement fees and closing costs that you ***cannot*** include in the basis of the property.

1) Fire insurance premiums.
2) Rent for occupancy of the property before closing.
3) Charges for utilities or other services related to occupancy of the property before closing.
4) Charges connected with getting a loan. The following are examples of these charges.
    a) Points (discount points, loan origination fees).
    b) Mortgage insurance premiums.
    c) Loan assumption fees.
    d) Cost of a credit report.
    e) Fees for an appraisal required by a lender.
5) Fees for refinancing a mortgage.

Points. If you pay points to obtain a loan (including a mortgage, second mortgage, line of credit, or a home equity loan), do not add the points to the basis of the related property. Generally, you deduct the points over the term of the loan. For more information on how to deduct points, see *Points* in chapter 8 of Publication 535, *Business Expenses.*

Points on home mortgage. Special rules may apply to points you and the seller pay when you obtain a mortgage to purchase your main home. If certain requirements are met, you can deduct the points in full for the year in which they are paid. If you deduct seller-paid points, reduce the basis of your home by that amount. For more information, see *Points* in Publication 936, *Home Mortgage Interest Deduction.*

Assumption of mortgage. If you buy property and assume (or buy subject to) an existing mortgage on the property, your basis includes the amount you pay for the property plus the amount to be paid on the mortgage you assume.

Example. If you buy a building for $20,000 and assume a mortgage of $80,000 on it, your basis is $100,000.

Constructing nonbusiness assets. If you build nonbusiness property (for example, your home) or have assets built for you, the expenses you pay for this construction are part of your basis. The following items are some examples of these expenses.

- The cost of land.
- The cost of labor and materials.
- Architect's fees.
- Building permit charges.
- Payments to contractors.
- Payments for rental equipment.
- Inspection fees.

In addition, if you own a business and use your employees, material, and equipment to construct a nonbusiness asset, your basis would also include the following items.

1) Employee compensation paid for the construction work.
2) Depreciation on your equipment while it is used in the construction.
3) Operating and maintenance costs for equipment used in the construction.
4) The cost of business supplies and materials used in the construction.

Do not deduct these expenses. You must capitalize them (include them in the asset's basis). Also, reduce your basis by any work opportunity credit, welfare-to-work credit, Indian employment credit, or empowerment zone employment credit allowable on the wages you pay in (1), above.

Do not include the value of your own labor, or any other labor you did not pay for, in the basis of any property you construct.

Business Assets

Terms you may need to know (see Glossary):

Amortization
Capital assets
Capital expenses
Capitalization
Depletion
Depreciation
Fair market value
Going concern value
Goodwill
Intangible property
Personal property
Recapture
Section 179 deduction
Section 197 intangibles
Tangible property

If you purchase property to use in your business, your basis is usually its actual cost to you. If you construct, create, or otherwise produce property, you must capitalize the costs as your basis. In certain circumstances, you may be subject to the uniform capitalization rules, next.

Uniform Capitalization Rules

The uniform capitalization rules specify the costs you add to basis in certain circumstances.

Who must use. You must use the uniform capitalization rules if you do any of the following in your trade or business or activity carried on for profit.

- Produce real or tangible personal property for use in the business or activity.
- Produce real or tangible personal property for sale to customers.
- Acquire property for resale.

You produce property if you construct, build, install, manufacture, develop, improve, create, raise or grow the property. Treat the property produced for you under a contract as produced by you up to the amount you pay or costs you otherwise incur for the property. Tangible personal property includes films, sound recordings, video tapes, books, or similar property.

Under the uniform capitalization rules, generally you must capitalize all direct costs and an allocable part of most indirect costs incurred during the year due to production or resale activities. You must include these costs in the basis of property you produce or in your inventory costs, rather than deduct them as a current expense. You recover these costs through depreciation, amortization, or cost of goods sold when you use, sell, or otherwise dispose of the property.

Any cost that you could not use to figure your taxable income for any tax year is not subject to the uniform capitalization rules.

Example. If you incur a business meal expense for which your deduction would be limited to 50% of the cost of the meal, that amount is subject to the uniform capitalization rules. The part of the cost that is not deductible is not subject to the uniform capitalization rules.

More information. For more information on the uniform capitalization rules, see the regulations under section 263A of the Internal Revenue Code and Publication 538, *Accounting Periods and Methods.*

Exceptions. The following are not subject to the uniform capitalization rules.

1) Property you produce that you do not use in your trade, business, or activity conducted for profit.

2) Qualified creative expenses you pay or incur as a free-lance (self-employed) writer, photographer, or artist that are otherwise deductible on your tax return.

3) Property you produce under a long-term contract, except for certain home construction contracts.

4) Research and experimental expenses allowable as a deduction under section 174 of the Internal Revenue Code.

5) Costs for personal property acquired for resale if your (or your predecessor's) average annual gross receipts for the 3 previous tax years do not exceed $10 million.

For other exceptions to the uniform capitalization rules, see section 1.263A-1(b) of the regulations.

For information on the special rules that apply to costs incurred in the business of farming, see chapter 7 of Publication 225, *Farmer's Tax Guide.*

Intangible Assets

Intangible assets include goodwill, patents, copyrights, trademarks, trade names, and franchises. The basis of an intangible asset is usually the cost to buy or create it. If you acquire multiple assets, for example a going business for a lump sum, see *Allocating the Basis,* later, to figure the basis of the individual assets. The basis of certain intangibles can be amortized. See chapter 12 of Publication 535 for information on the amortization of these costs.

Patents. The basis of a patent you get for your invention is the cost of development, such as research and experimental expenditures, drawings, working models, and attorneys' and governmental fees. If you deduct the research and experimental expenditures as current business expenses, you cannot include them in the basis of the patent. The value of the inventor's time spent on an invention is not part of the basis.

Copyrights. If you are an author, the basis of the copyright for your work usually will be your cost of getting the copyright plus copyright fees, attorneys' fees, clerical assistance, and the cost of plates that remain in your possession. Do not include in the basis the value of your time as the author, or any other person's time you did not pay for.

Franchises, trademarks, and trade names. If you buy a franchise, trademark, or trade name, the basis is its cost, unless you can deduct your payments as a business expense.

Allocating the Basis

If you buy multiple assets for a lump sum, allocate the amount you pay to each of the assets you receive. Make this allocation to figure your basis for depreciation and gain or loss on a later disposition of any of these assets. See *Trade or Business Acquired,* later.

Group of Assets Acquired

If you buy multiple assets for a lump sum, you and the seller may agree to a specific allocation of the purchase price to each asset in the sales contract. If this allocation is based on the value of each asset and you and the seller have adverse tax interests, the allocation generally will be accepted. However, see *Trade or Business Acquired,* next.

Trade or Business Acquired

If you acquire a group of assets that is a trade or business, allocate the purchase price to the various assets acquired.

Make the allocation among the assets in proportion to (but not in excess of) their fair market value (FMV) on the purchase date in the following order.

1) Cash, demand deposits, and similar accounts.

2) Certificates of deposit, U.S. Government securities, readily marketable stock or securities, and foreign currency.

3) All other assets except section 197 intangibles.

4) Section 197 intangibles (other than goodwill and going concern value).

5) Section 197 intangibles in the nature of goodwill and going concern value.

Agreement. If you and the seller agree in writing to allocate the consideration, or the FMV of any asset, the agreement is binding on both you and the seller unless the IRS determines that the amounts are not appropriate.

Reporting requirement. Both the buyer and seller of a trade or business must report to the IRS the allocation of the sales price among section 197 intangibles and the other business assets. Use Form 8594 to provide this information. The buyer and seller should each attach Form 8594 to their federal income tax returns for the year in which the sale occurred.

Land and Buildings

If you buy buildings and the land on which they stand for your business and you pay a lump sum for it, allocate the basis of the whole property among the land and buildings so you can figure the depreciation allowable on the buildings.

Figure the basis of each asset by multiplying the lump sum you paid by a fraction. The numerator of the fraction is the FMV of that asset and the denominator is the FMV of the whole property at the time you get the property. If you are not certain of the FMV of the land and buildings, you may allocate the basis among them based on their assessed values for real estate tax purposes.

Demolition of building. Add demolition costs and other losses incurred for the demolition of any building to the basis of the land on which the demolished building was located. Do not claim them as a current deduction.

Modification of building. A modification of a building will not be treated as a demolition if the following conditions are satisfied.

- 75 percent or more of the existing external walls of the building are retained in place as internal or external walls.
- 75 percent or more of the existing internal structural framework of the building is retained in place.

If the building is a ***certified historic structure*** the modification must also be part of a certified rehabilitation.

If these conditions are met, add the costs of the modifications to the basis of the building.

Subdivided lots. If you buy a tract of land and subdivide it, you must determine the basis of each lot. This is necessary because you must figure the gain or loss on the sale of each individual lot. As a result, you do not recover your entire cost in the tract until you have sold all of the lots.

To determine the basis of an individual lot, multiply the total cost of the tract by a fraction. The numerator (top part) is the FMV of the lot and the denominator (bottom part) is the FMV of the entire tract.

Future improvement costs. If you are a developer and sell subdivided lots before the development work is completed, you can (with IRS consent) include in the basis of the properties sold an allocation of the estimated future cost for common improvements. See Revenue Procedure 92–29 for more information, including an explanation of the procedures for getting consent from the IRS.

Use of erroneous cost basis. If you made a mistake in figuring the cost basis of subdivided lots that you sold in previous years, you cannot correct the mistake for years for which the statute of limitations has expired. Figure the basis of any remaining lots by allocating the correct original cost basis of the entire tract among the original lots.

Example. You bought a tract of land to which you assigned a cost of $15,000. You subdivided the land into 15 building lots of equal size and equitably divided your basis so that each lot had a basis of $1,000. You treated the sale of each lot as a separate transaction and figured gain or loss separately on each sale.

Several years later you determine that your original basis in the tract was $22,500 and not $15,000. You sold eight lots using $8,000 of basis in years for which the statute of limitations has expired. You now can take $1,500 of basis into account for figuring gain or loss only on the sale of each of the remaining seven lots ($22,500 basis divided among all 15 lots). You cannot refigure (to $1,500) the basis of the eight lots sold in tax years barred by the statute of limitations.

Adjusted Basis

Before figuring gain or loss on a sale, exchange, or other disposition of property, or figuring allowable depreciation, depletion, or amortization, you must usually make certain adjustments (increases and decreases) to the basis of the property. The result of these adjustments to the basis is the adjusted basis.

Table 1. **Examples of Increases and Decreases to Basis**

Increases to Basis	Decreases to Basis
Capital improvements: Putting an addition on your home Replacing an entire roof Paving your driveway Installing central air conditioning Rewiring your home	Exclusion from income of subsidies for energy conservation measures Casualty or theft loss deductions and insurance reimbursements Credit for qualified electric vehicles Section 179 deduction Deduction for clean-fuel vehicles and clean-fuel vehicle refueling property Depreciation Nontaxable corporate distributions
Assessments for local improvements: Water connections Sidewalks Roads	
Casualty losses: Restoring damaged property	
Legal fees: Cost of defending and perfecting a title	
Zoning costs	

Increases to Basis

Increase the basis of any property by all items properly added to a capital account. These include the cost of any improvements having a useful life of more than 1 year and amounts spent after a casualty to restore the damaged property.

Rehabilitation expenses also increase basis. However, you must subtract any rehabilitation credit allowed for these expenses before you add them to your basis. If you have to recapture any of the credit, increase your basis by the amount of the recapture.

If you make additions or improvements to business property, keep separate accounts for them. Also, depreciate the basis of each according to the depreciation rules in effect when you place the addition or improvement in service. For more information, see Publication 946.

Some items that increase the basis of property are listed next.

- The cost of extending utility service lines to the property.
- Legal fees, such as the cost of defending and perfecting title.
- Legal fees for obtaining a decrease in an assessment levied against property to pay for local improvements.
- Zoning costs.
- The capitalized value of a redeemable ground rent.

Assessments for Local Improvements

Add assessments for items such as streets and sidewalks to the basis of the property assessed if they increase the value of the property. Do not deduct them as taxes. However, you can deduct as taxes assessments for maintenance, repair, or meeting interest charges on the improvements.

Example. If your city changes the street in front of your store into an enclosed pedestrian mall, and assesses you and other affected landowners for the cost of the conversion, add the assessment to your property's basis. In this example, the amount of the assessment is a depreciable asset.

Deducting vs. Capitalizing Costs

Do not add to your basis costs you can deduct as current expenses. However, you can choose either to deduct or to capitalize certain other costs. If you capitalize these costs, include them in your basis. If you deduct them, do not include them in your basis. (See *Uniform Capitalization Rules,* earlier.)

The costs you can choose to deduct or to capitalize include the following items.

- Carrying charges, such as interest and taxes, that you pay to own property, except carrying charges that must be capitalized under the uniform capitalization rules.
- Research and experimentation costs.
- Intangible drilling and development costs for oil, gas, and geothermal wells.
- Exploration costs for new mineral deposits.
- Mining development costs for a new mineral deposit.
- The costs of establishing, maintaining, or increasing the circulation of a newspaper or other periodical.
- The cost of removing architectural and transportation barriers to people with disabilities and the elderly. If you claim the disabled access credit, you must reduce the amount you deduct or capitalize by the amount of the credit.

For more information about deducting or capitalizing costs, see chapter 11 in Publication 535.

Decreases to Basis

Some items that reduce the basis of your property are listed next.

- The section 179 deduction.
- The deduction for clean-fuel vehicles and clean-fuel vehicle refueling property.
- Nontaxable corporate distributions.
- Deductions previously allowed (or allowable) for amortization, depreciation, and depletion.

- Exclusion from income of subsidies for energy conservation measures.
- Credit for qualified electric vehicles.
- Gain from the sale of your home on which tax was postponed.
- Investment credit (part or all of credit) taken.
- Casualty and theft losses and insurance reimbursements.
- Certain canceled debt excluded from income.
- Rebates received from a manufacturer or seller.
- Easements.
- Gas-guzzler tax.
- Tax credit or refund for buying a diesel-powered highway vehicle.
- Adoption tax benefits.

Some of these decreases to basis are discussed next.

Casualty and Theft Losses

If you have a casualty or theft loss, decrease the basis in your property by the amount of any insurance or other reimbursement you receive and by any deductible loss not covered by insurance. However, increase your basis by amounts you spend after a casualty to restore the damaged property. For more information on casualty and theft losses, see Publication 547, *Casualties, Disasters, and Thefts.*

Easements

The amount you receive for granting an easement is generally considered to be from the sale of an interest in your real property. It reduces the basis of the affected part of the property. If the amount received is more than the basis of the part of the property affected by the easement, reduce your basis in that part to zero and treat the excess as a recognized gain.

Credit for Qualified Electric Vehicles

If you claim the credit for a qualified electric vehicle, you must reduce your basis in that vehicle by the lesser of the following amounts.

- $4,000.
- 10% of the vehicle's cost.

This reduction amount applies even if the credit allowed is less than that amount. For more information on this credit, see chapter 15 in Publication 535.

Gas-Guzzler Tax

Decrease the basis in your car by the gas-guzzler (fuel economy) tax if you begin using the car within 1 year of the date of its first sale for ultimate use. This rule also applies to someone who later buys the car and begins using it not more than 1 year after the original sale for ultimate use. If the car is imported, the one-year period begins on the date of entry or withdrawal of the car from the warehouse if that date is later than the date of the first sale for ultimate use.

Diesel-Powered Vehicle

If you received an income tax credit or refund for a diesel-powered highway vehicle that you purchased before August 21, 1996, reduce your basis in that vehicle by the credit or refund allowable.

Section 179 Deduction

If you take the section 179 deduction for all or part of the cost of business property, decrease the basis of the property by the deduction. For more information about the section 179 deduction, see Publication 946.

Deduction for Clean-Fuel Vehicles and Clean-Fuel Vehicle Refueling Property

If you take the deduction for clean-fuel vehicles or clean-fuel vehicle refueling property, you must decrease the basis of the property by the amount of the deduction. For more information on these deductions, see chapter 15 in Publication 535.

Exclusion from Income of Subsidies for Energy Conservation Measures

If you received a subsidy from a public utility company for the purchase or installation of any energy conservation measure for a dwelling unit, you can exclude it from income. Reduce the basis of the property for which you received the subsidy by the excluded amount. For more information on this subsidy, see Publication 525.

Depreciation

Decrease the basis of your property by the depreciation you deducted or could have deducted on your tax returns under the method of depreciation you selected. If you took less depreciation than you could have under the method you selected, decrease the basis by the amount you could have taken under that method. If you did not take a depreciation deduction, then make adjustments to basis for depreciation you could have taken.

If you deducted more depreciation than you should have, decrease your basis as follows. Decrease it by an amount equal to the depreciation you should have deducted, as well as by the part of the excess depreciation you deducted that actually reduced your tax liability for any year.

In decreasing your basis for depreciation, take into account the amount deducted on your tax returns as depreciation, and any depreciation you must capitalize under the uniform capitalization rules.

For information on figuring depreciation, see Publication 946.

If you are claiming depreciation on a car you use in your trade or business, see Publication 463. If the car is not used more than 50% for business during the tax year, you may have to recapture excess depreciation. Include the excess depreciation in your gross income and add it to your basis in the property. For information on the computation of excess depreciation, see chapter 4 in Publication 463.

Canceled Debt Excluded from Income

If a debt you owe is canceled or forgiven, other than as a gift or bequest, you generally must include the canceled amount in your gross income for tax purposes. A debt includes any indebtedness for which you are liable or which attaches to property you hold. You can exclude your canceled debt from income in the following situations.

1) The cancellation takes place in a title 11 bankruptcy case or when you are insolvent.
2) The canceled debt is qualified farm debt.
3) The canceled debt is qualified real property business indebtedness (provided you are not a C corporation).

If you exclude from income canceled debt under situation (1) or (2), you may have to reduce the basis of your depreciable and nondepreciable property. However, for situation (3), you ***must*** reduce the basis of your depreciable property by the excluded amount.

For more information on canceled debt in a bankruptcy case or during insolvency, see Publication 908, *Bankruptcy Tax Guide.* For more information on canceled debt that is qualified farm debt, see chapter 4 in Publication 225. For more information on canceled debt that is qualified real property business debt, see chapter 5 in Publication 334, *Tax Guide for Small Business.*

Gain from Sale of Home on Which Tax Was Postponed

If you postponed gain from the sale of your main home before May 7, 1997, you must reduce the basis of your new home by the amount of the postponed gain. For more information on the rules for the sale of a home, see Publication 523.

Adoption Tax Benefits

If you claim an adoption credit for the cost of improvements that you added to the basis of your home, decrease the basis of your home by the credit allowed. This also applies to amounts that you received under an employer's adoption assistance program and excluded from income. For more information on these benefits, see Publication 968, *Tax Benefits for Adoption.*

Example

In January 1994, you paid $80,000 for real property to be used as a factory. You also paid commissions of $2,000 and title search and legal fees of $600. You allocated the total cost of $82,600 between the land and the building—$10,325 for the land and $72,275 for the building. Immediately, you spent $20,000 in remodeling the building before you placed it in service. You were allowed depreciation of $14,526 for the years 1994 through 1998. In 1997 you had a casualty loss that was not covered by insurance of $5,000 on the building from a fire. You claimed this loss as a deduction and spent $5,500 to repair the fire damages. The adjusted basis of the building on January 1, 1999, is figured as follows:

Original cost of building, including fees and commissions		$72,275
Adjustments to basis:		
Add:		
Improvements		20,000
Repair of fire damage		5,500
		$97,775
Subtract:		
Depreciation	$14,526	
Deducted casualty loss	5,000	19,526
Adjusted basis on January 1, 1999		**$78,249**

The basis of the land, $10,325, remains unchanged. It is not affected by any of the above adjustments, which affect only the basis of the building.

Other Basis

There are many times when you cannot use cost as basis. In these cases, the FMV or the adjusted basis of property may be used. Adjusted basis is defined in the preceding discussion, and FMV is defined next.

Fair market value (FMV). FMV is the price at which the property would change hands between a buyer and a seller, neither having to buy or sell, and both having reasonable knowledge of all necessary facts. Sales of similar property, on or about the same date, may be helpful in figuring the property's FMV.

Property Received for Services

If you receive property for services, include the property's FMV in income. The amount you include in income becomes your basis. If the services were performed for a price agreed on beforehand, it will be accepted as the FMV of the property if there is no evidence to the contrary.

Bargain Purchases

A bargain purchase is a purchase of an item for less than its FMV. If, as compensation for services, you purchase goods or other property at less than FMV, include the difference between the purchase price and FMV of the property in your income. Your basis in the property is its FMV (your purchase price plus the amount you include in income).

If the difference between your purchase price and the FMV represents a ***qualified employee discount,*** do not include the amount in income. However, your basis in the property is still its FMV.

Restricted Property

If you receive property for your services and the property is subject to certain restrictions, your basis in the property is its FMV when it becomes substantially vested, unless you make the election discussed later. Property becomes substantially vested when your rights in the property or the rights of any person to whom you transfer the property are not subject to a substantial risk of forfeiture.

There is substantial risk of forfeiture when the rights to full enjoyment of the property depend on the future performance of substantial services by any person.

When the property becomes substantially vested, include the FMV, less any amount you paid for the property, in income.

Example. Your employer gives you stock for services performed under the condition that you will have to return the stock unless you complete 5 years of service. The stock is under a substantial risk of forfeiture and is not substantially vested when you receive it. You need not report any income until you have completed the 5 years of service that satisfy the condition.

Fair market value. Figure the FMV of property you received without considering any restriction except one that by its terms will never end.

Example. For services you performed, you received stock from your employer. If you want to sell the stock while still employed, you must sell the stock to your employer at book value. At your retirement or death, you or your estate must offer to sell the stock to your employer at its book value. This is a restriction that by its terms will never end and you consider it when you figure the FMV.

Election. You may choose to include in your gross income the FMV of the property at the time of transfer, less any amount you paid for it. If you make this choice, the substantially vested rules do not apply. Your basis is the amount you paid plus the amount you included in your income.

See the discussion of *Restricted Property Received for Services* in Publication 525 for more information.

Taxable Exchanges

A taxable exchange is one in which the gain is taxable or the loss is deductible. If you receive property in exchange for other property in a taxable exchange, the basis of property you receive is usually its FMV at the time of the exchange.

Involuntary Conversions

If you receive property as a result of an involuntary conversion, such as a casualty, theft, or condemnation, you may figure the basis of the replacement property you receive using the basis of the converted property.

Similar or related property. If you receive property that is similar or related in service or use to the converted property, the replacement property's basis is the old property's basis on the date of the conversion with the following adjustments.

1) Decrease the basis by the following items.
   a) Any loss you recognize on the conversion.
   b) Any money you receive that you do not spend on similar property.
2) Increase the basis by the following items.
   a) Any gain you recognize on the conversion.
   b) Any cost of acquiring the replacement property.

Money or property that is not similar or related. If you receive money or property that is not similar or related in service or use to the converted property, and you buy replacement property that is similar or related in service or use to the converted property, the basis of the new property is its cost, decreased by the amount of gain that is not recognized on the conversion.

Example. The state condemned your property. The property had an adjusted basis of $26,000, and the state paid you $31,000 for it. You realized a gain of $5,000 ($31,000 – $26,000). You bought replacement property that is similar in use to the converted property for $29,000. You recognize a gain of $2,000 ($31,000 – $29,000), the unspent part of the payment from the state. Your gain not recognized is $3,000, the difference between the $5,000 realized gain and the $2,000 recognized gain. The basis of the new property is figured as follows:

Cost of replacement property	$29,000
Minus: Gain not recognized	3,000
Basis of the replacement property	**$26,000**

Allocating the basis. If you buy more than one piece of replacement property, allocate your basis among the properties based on their respective costs.

Example. The state in the previous example condemned your unimproved real property and the replacement property you bought was improved real property with both land and buildings. Allocate the replacement property's $26,000 basis between land and buildings based on their respective costs.

More information. For more information about condemnations, see *Involuntary Conversions* in Publication 544. For more information about casualty and theft losses, see Publication 547.

Nontaxable Exchanges

Terms you may need to know (see Glossary):

Intangible property
Like-class property
Like-kind property
Personal property
Real property
Tangible property

A nontaxable exchange is an exchange in which any gain is not taxed and any loss cannot be deducted. If you receive property in a nontaxable exchange, its basis is generally the same as the basis of the property you transferred.

Like-Kind Exchanges

The exchange of property for the same kind of property is the most common type of nontaxable exchange.

To qualify as a like-kind exchange, both the property you transfer and the property you receive must be held by you for business or investment purposes. There must be an exchange of like property. For more information, see *Like-Kind Exchanges* in Publication 544.

The basis of the property you receive is generally the same as the basis of the property you gave up.

Example. You exchange real estate (adjusted basis $50,000, FMV $80,000) held for investment for other real estate (FMV $80,000) held for investment. Your basis in the new property is the same as the basis of the old ($50,000).

Exchange expenses. Exchange expenses are generally the closing costs that you pay. They include such items as brokerage commissions, attorney fees, deed preparation fees, etc. Add them to the basis of the like-kind property received.

Property plus cash. If you trade property in a like-kind exchange and also pay money, the basis of the property received is the basis of the property you gave up increased by the money paid.

Example. You trade in a truck (adjusted basis $3,000) for another truck (FMV $7,500) and pay $4,000. Your basis in the new truck is $7,000 (the $3,000 basis of the old truck plus the $4,000 paid).

Special rules for related persons. If a like-kind exchange is made directly or indirectly between related persons and either party disposes of the property within 2 years after the exchange, the exchange is disqualified from like-kind exchange treatment. Each person must report any gain or loss not recognized on the original exchange. Each person reports it on the tax return filed for the year in which the later disposition occurred. If this special rule applies, the basis in the property received in the original exchange will be its fair market value.

These rules generally do not apply to the following kinds of property dispositions.

1) Dispositions due to the death of either related person.
2) Involuntary conversions.
3) Dispositions in which neither the original exchange nor the subsequent disposition had as a main purpose the avoidance of federal income tax.

Related persons. Generally, related persons are ancestors, lineal descendants, brothers and sisters (whole or half), and a spouse.

For other related persons (for example, two corporations, an individual and a corporation, a grantor and fiduciary, etc.), see *Nondeductible Loss* in chapter 2 of Publication 544.

Exchange of businesses. Exchanging the assets of one business for the assets of another business is a multiple property exchange. For information on determining basis, see *Multiple Property Exchanges* in Publication 544.

Partially Nontaxable Exchange

A partially nontaxable exchange is an exchange in which you receive unlike property or money in addition to like property. The basis of the property you receive is the basis of the property you gave up, with the following adjustments.

1) Decrease the basis by the following items.
   a) Any money you receive.
   b) Any loss you recognize on the exchange.
2) Increase the basis by the following items.
   a) Any additional costs you incur.
   b) Any gain you recognize on the exchange.

If the other party to the transaction assumes any of your liabilities, or if you transfer property subject to a liability, you will be treated as if you received money in the amount of the liability.

Allocate the basis among the properties, other than money, you received in the exchange. In making this allocation, the basis of the unlike property is its FMV on the date of the exchange. The remainder is the basis of the like property.

Example 1. You exchange a truck (adjusted basis $6,000) for a new truck (FMV $5,200) and $1,000 cash. You have a recognized gain of $200 ($6,200 – $6,000). Your basis in the new truck is:

Adjusted basis of old truck	$6,000
Minus: Cash received	1,000
	$5,000
Plus: Gain recognized	200
Basis of new truck	**$5,200**

Example 2. You had an adjusted basis of $15,000 in real estate you held for investment. You exchange it for other real estate to be held for investment with an FMV of $12,500, a truck with an FMV of $3,000, and $1,000 cash. You have a gain of $1,500 ($16,500 – $15,000) recognized on the exchange. Your basis in the properties you received is:

Adjusted basis of real estate transferred	$15,000
Minus: Cash received	1,000
	$14,000
Plus: Gain recognized	1,500
Total basis of properties received	**$15,500**

Allocate the total basis of $15,500 between the truck and the real estate. The basis of the truck is its FMV, $3,000, and the basis of the real estate is the remainder, $12,500.

Sale and Purchase

If you sell property and buy similar property in two mutually dependent transactions, you may have to treat the sale and purchase as a single nontaxable exchange. Treat the transaction as an exchange no matter how it is carried out. You cannot avoid this rule by using a subsidiary in the transaction.

Example. You are a salesperson and you use one of your cars 100% for business. You have used this car in your sales activities for 2 years and have depreciated it. Your adjusted basis in the car is $22,600 and its FMV is $23,100. You are interested in a new car, which sells for $28,000. If you trade your old car and pay $4,900 for the new one, your basis for depreciation for the new car would be $27,500 ($4,900 plus the $22,600 basis of your old car). However, you want a higher basis for depreciating the new car, so you agree to pay the dealer $28,000 for the new car if he will pay you $23,100 for your old car. Since the sale and purchase are dependent on each other, you are treated as if you had exchanged your old car for the new one and paid $4,900 ($28,000 – $23,100). Your basis for depreciating the new car is $27,500, which is the same as it would be if you traded the old car.

Partial Business Use of Property

If you have property used partly for business and partly for personal use, and you exchange it in a nontaxable exchange for property to be used wholly or partly in your business, the basis of the property you receive is figured as if you exchanged two properties. The first is an exchange of like-kind property. The second is personal-use property on which gain is recognized and loss is not recognized.

First, figure your adjusted basis in the property you transfer as if you transferred two separate properties. Figure the adjusted basis of each part of the property by taking into account any adjustments to basis. Deduct the depreciation you took or could have taken from the adjusted basis of the business part. Then figure the amount realized for your property and allocate it to the business and nonbusiness parts of the property you transferred.

The business part of the property is permitted to be exchanged tax free. However, recognize any gain from the exchange of the nonbusiness part. You are deemed to have received in exchange for the nonbusiness part an amount equal to its FMV on the date of the exchange. The basis of the property you acquired is the total basis of the property transferred (adjusted to the date of the exchange), increased by any gain recognized on the nonbusiness part.

TIP *If the nonbusiness part of the property you transferred is your main home, you may qualify to exclude from income all or part of any gain on that part. For more information, see Publication 523.*

Traded car used partly in business. If you trade in a car that you used partly in your business for another car that you will use in your business, your basis for depreciating the new car is not the same as your basis for figuring a gain or loss on its sale.

For information on figuring your basis for depreciation, see Publication 463.

Property Transferred From a Spouse

The basis of property transferred to you or transferred in trust for your benefit by your spouse (or former spouse if the transfer is incident to divorce), is the same as the transferor's adjusted basis. However, adjust your basis for any gain recognized by the transferor on a property transferred in trust. This rule applies only to a transfer of property in trust in which the liabilities assumed, plus the liabilities to which the property is subject, are more than the adjusted basis of the property transferred.

If the property transferred to you is a series E, series EE or series I United States savings bond, the transferor must include in income the interest accrued to the date of transfer. Your basis in the bond immediately after the transfer is equal to the transferor's basis increased by the interest income includable in the transferor's income. For more information on these bonds, see Publication 550.

The transferor must supply you with records necessary to determine the adjusted basis and holding period of the property as of the date of transfer.

For more information, see Publication 504, *Divorced or Separated Individuals.*

Property Received as a Gift

To figure the basis of property you receive as a gift, you must know its adjusted basis (defined earlier) to the donor just before it was given to you, its FMV at the time it was given to you, and any gift tax paid on it.

FMV Less Than Donor's Adjusted Basis

If the FMV of the property is less than the donor's adjusted basis, your basis depends on whether you have a gain or a loss when you dispose of the property. Your basis for figuring gain is the same as the donor's adjusted basis plus or minus any required adjustment to basis while you held the property (see *Adjusted Basis,* earlier). Your basis for figuring loss is its FMV at the time you received the gift plus or minus any required adjustment to basis while you held the property (see *Adjusted Basis,* earlier).

If you use the donor's adjusted basis for figuring a gain and get a loss, and then use the FMV for figuring a loss and have a gain, you have neither gain nor loss on the sale or disposition of the property.

Example. You received an acre of land as a gift. At the time of the gift, the acre had an FMV of $8,000. The donor's adjusted basis was $10,000. After you received the property, no events occurred to increase or decrease your basis in it. If you later sell the property for $12,000, you will have a $2,000 gain because you must use the donor's adjusted basis ($10,000) at the time of the gift as your basis to figure gain. If, however, you sell the property for $7,000, you will have a $1,000 loss because you must use the FMV ($8,000) at the time of the gift as your basis to figure loss.

If the sales price is between $8,000 and $10,000, you have neither gain nor loss. For instance, if the sales price was $9,000 and you tried to figure a gain using the donor's adjusted basis ($10,000), you would get a $1,000 loss. If you then tried to figure a loss using the FMV ($8,000), you would get a $1,000 gain.

Business property. If you hold the gift as business property, your basis for figuring any depreciation, depletion, or amortization deduction is the same as the donor's adjusted basis plus or minus any required adjustments to basis while you hold the property.

FMV Equal to or More Than Donor's Adjusted Basis

If the FMV of the property is equal to or greater than the donor's adjusted basis, your basis is the donor's adjusted basis at the time you received the gift. Increase your basis by all or part of any gift tax paid, depending on the date of the gift.

Also, for figuring gain or loss from a sale or other disposition of the property or for figuring depreciation, depletion, or amortization deductions on business property, you must increase or decrease your basis (the donor's adjusted basis) by any required adjustments to basis while you held the property. See *Adjusted Basis,* earlier.

Gift received before 1977. If you received a gift before 1977, increase your basis in the gift (the donor's adjusted basis) by any gift tax paid on it. However, do not increase your basis above the FMV of the gift at the time it was given to you.

Example 1. You were given a house in 1976 with an FMV of $21,000. The donor's adjusted basis was $20,000. The donor paid a gift tax of $500. Your basis is $20,500, the donor's adjusted basis plus the gift tax paid.

Example 2. If, in Example 1, the gift tax paid had been $1,500, your basis would be $21,000. This is the donor's adjusted basis plus the gift tax paid, limited to the FMV of the house at the time you received the gift.

Gift received after 1976. If you received a gift after 1976, increase your basis in the gift (the donor's adjusted basis) by the part of the gift tax paid on it that is due to the net increase in value of the gift. Figure the increase by multiplying the gift tax paid by a fraction. The numerator (top part) of the fraction is the net increase in value of the gift, and the denominator (bottom part) is the amount of the gift.

The net increase in value of the gift is the FMV of the gift minus the donor's adjusted basis. The amount of the gift is its value for gift tax purposes after reduction by any annual exclusion and marital or charitable deduction that applies to the gift. For information on the gift tax, see Publication 950, *Introduction to Estate and Gift Taxes.*

Example. In 1999, you received a gift of property from your mother that had an FMV of $50,000. Her adjusted basis was $20,000. The amount of the gift for gift tax purposes was $40,000 ($50,000 minus the $10,000 annual exclusion). She paid a gift tax of $9,000. Your basis, $26,750, is figured as follows:

Fair market value	$50,000
Minus: Adjusted basis	20,000
Net increase in value	$30,000
Gift tax paid	$9,000
Multiplied by ($30,000 ÷ $40,000)	.75
Gift tax due to net increase in value	$6,750
Adjusted basis of property to your mother	20,000
Your basis in the property	**$26,750**

Inherited Property

Your basis in property you inherit from a decedent is generally one of the following.

1) The FMV of the property at the date of the individual's death.

2) The FMV on the alternate valuation date, if the personal representative for the estate chooses to use alternate valuation. For information on the alternate valuation date, see the instructions for Form 706.

3) The value under the special-use valuation method for real property used in farming or other closely held business, if chosen for estate tax purposes. This method is discussed later.

4) The decedent's adjusted basis in land to the extent of the value that is excluded from the decedent's taxable estate as a qualified conservation easement.

If a federal estate tax return does not have to be filed, your basis in the inherited property is its appraised value at the date of death for state inheritance or transmission taxes.

Appreciated property. The above rule does not apply to appreciated property you receive from a decedent if you or your spouse originally gave the property to the decedent within 1 year before the decedent's death. Your basis in this property is the same as the decedent's adjusted basis in the property immediately before his or her death, rather than its FMV. Appreciated property is any property whose FMV on the day it was given to the decedent is more than its adjusted basis.

Community Property

In community property states (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin), husband and wife are each usually considered to own half the community property. When either spouse dies, the total value of the community property, even the part belonging to the surviving spouse, generally becomes the basis of the entire property. For this rule to apply, at least half the value of the community property interest must be includable in the decedent's gross estate, whether or not the estate must file a return.

For example, you and your spouse owned community property that had a basis of $80,000. When your spouse died, at least half the FMV of the community interest was includable in your spouse's estate. The FMV of the community interest was $100,000. The basis of your half of the property is $50,000 (one half of the $100,000 FMV). The basis of the other half to your spouse's heirs is also $50,000.

For more information on community property, see Publication 555.

Property Held by Surviving Tenant

The following example explains the rule for the basis of property held by a surviving tenant in a joint tenancy or tenancy by the entirety.

Example. John and Jim owned, as joint tenants with right of survivorship, business property that they purchased for $30,000. John furnished two-thirds of the purchase price and Jim furnished one-third. Depreciation deductions allowed before John's death were $12,000. Under local law, each had a half interest in the income from the property. At the date of John's death, the property had an FMV of $60,000, two-thirds of which is includable in John's estate. Jim figures his basis in the property at the date of John's death as follows:

Interest Jim bought with his own funds—$\frac{1}{3}$ of $30,000 cost	$10,000	
Interest Jim received on John's death—$\frac{2}{3}$ of $60,000 FMV	40,000	$50,000
Minus: $\frac{1}{2}$ of $12,000 depreciation before John's death		6,000
Jim's basis at the date of John's death		**$44,000**

If Jim had not contributed any part of the purchase price, his basis at the date of John's death would be $54,000. This is figured by subtracting from the $60,000 FMV, the $6,000 depreciation allocated to Jim's half interest before the date of death.

If, under local law, Jim had no interest in the income from the property and if he contributed no part of the purchase price, his basis at John's death would be $60,000. This $60,000 is the FMV of the property.

Qualified Joint Interest

Include one-half of the value of a qualified joint interest in the decedent's gross estate. It does not matter how much each spouse contributed to the purchase price. Also, it does not matter which spouse dies first.

A qualified joint interest is any interest in property held by husband and wife as either of the following.

- Tenants by the entirety.
- Joint tenants with right of survivorship, if husband and wife are the only joint tenants.

Basis. As the surviving spouse, your basis in property that you owned with your spouse as a qualified joint interest is the cost of your half of the property with some adjustments. Decrease the cost by any deductions allowed to you for depreciation and for depletion. Increase the reduced cost by your basis in the half you inherited.

Farm or Closely Held Business

Under certain conditions, when a person dies the executor or personal representative of that person's estate may choose to value the qualified real property on other than its FMV. If so, the executor or personal representative values the qualified real property based on its use as a farm or its use in a closely held business. If the executor or personal representative chooses this method of valuation for estate tax purposes, that value is the basis of the property for the heirs. The qualified heirs should be able to get the necessary value from the executor or personal representative of the estate.

If you are a qualified heir who received special-use valuation property, your basis in the property is the estate's or trust's basis in that property immediately before the distribution. Increase your basis by any gain recognized by the estate or trust because of post-death appreciation. Post-death appreciation is the property's FMV on the date of distribution minus the property's FMV either on the date of the individual's death or the alternate valuation date. Figure all FMVs without regard to the special-use valuation.

You can elect to increase your basis in special-use valuation property if it becomes subject to the additional estate tax. This tax is assessed if, within 10 years after the death of the decedent, you transfer the property to a person who is not a member of your family or the property stops being used as a farm or in a closely held business.

To increase your basis in the property, you must make an irrevocable election and pay interest on the additional estate tax figured from the date 9 months after the decedent's death until the date of the payment of the additional estate tax. If you meet these requirements, increase your basis in the property to its FMV on the date of the decedent's death or the alternate valuation date. The increase in your basis is considered to have occurred immediately before the event that results in the additional estate tax.

You make the election by filing with Form 706-A a statement that does all of the following.

1) Contains your (and the estate's) name, address, and taxpayer identification number.
2) Identifies the election as an election under section 1016(c) of the Internal Revenue Code.
3) Specifies the property for which the election is made.
4) Provides any additional information required by the Form 706-A instructions.

For more information, see the instructions for Form 706 and Form 706-A.

Property Changed to Business or Rental Use

When you hold property for personal use and change it to business use or use it to produce rent, you must figure its basis for depreciation. An example of changing property held for personal use to business use would be renting out your former main home.

Basis for depreciation. The basis for depreciation is the lesser of the following amounts.

- The FMV of the property on the date of the change.
- Your adjusted basis on the date of the change.

Example. Several years ago you paid $160,000 to have your home built on a lot that cost you $25,000. Before changing the property to rental use last year, you paid $20,000 for permanent improvements to the house and claimed a $2,000 casualty loss deduction for damage to the house. Because land is not depreciable, you can only include the cost of the house when figuring the basis for depreciation.

Your adjusted basis in the house when you change its use is $178,000 ($160,000 + $20,000 − $2,000). On the date of change in use, your property has an FMV of $180,000, of which $15,000 is for the land and $165,000 is for the house. The basis for figuring depreciation on the house is the FMV on the date of change ($165,000), because it is less than your adjusted basis ($178,000).

Sale of property. If you later sell or dispose of the property, the basis of the property you use will depend on whether you are figuring gain or loss.

Gain. The basis for figuring a gain is your adjusted basis when you sell the property.

Example. Assume the same facts as in the previous example, except that you sell the property at a gain after being allowed depreciation deductions of $37,500. Your adjusted basis for figuring gain is $165,500 ($178,000 + $25,000 (land) − $37,500).

Loss. Figure the basis for a loss starting with the smaller of your adjusted basis or the FMV of the property at the time of the change to business/rental use.

Example. Assume the same facts as in the previous example, except that you sell the property at a loss after being allowed depreciation deductions of $37,500. In this case, you would start with the FMV ($180,000) on the date of the change to rental use, because it is less than the adjusted basis of $203,000 ($178,000 + $25,000) on that date. Reduce that amount ($180,000) by the amount of depreciation deductions to arrive at a basis for loss of $142,500 ($180,000–$37,500).

How To Get More Information

You can order free publications and forms, ask tax questions, and get more information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Free tax services. To find out what services are available, get Publication 910, *Guide to Free Tax Services*. It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

Personal computer. With your personal computer and modem, you can access the IRS on the Internet at **www.irs.ustreas.gov**. While visiting our Web Site, you can select:

- *Frequently Asked Tax Questions* to find answers to questions you may have.
- *Fill-in Forms* to complete tax forms online.
- *Forms and Publications* to download forms and publications or search publications by topic or keyword.
- *Tax Info For You* to view Internal Revenue Bulletins and Cumulative Bulletins published in the last few years.
- *Tax Regs In English* to search regulations and the Internal Revenue Code (under the *United States Code (USC)).*
- *Comments & Help* to e-mail us with comments about the site or with tax questions.
- *Digital Dispatch* and *IRS Local News Net* to receive our electronic newsletters on hot tax issues and news.

You can also reach us with your computer using any of the following.

- Telnet at **iris.irs.ustreas.gov**
- File Transfer Protocol at **ftp.irs.ustreas.gov**
- Direct dial (by modem) **703–321–8020**

TaxFax Service. Using the phone attached to your fax machine, you can receive forms and instructions by calling **703–368–9694.** Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.

Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call **1–800–829–3676** to order current and prior year forms, instructions, and publications.

- *Asking tax questions.* Call the IRS with your tax questions at **1–800–829–1040**.
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **1–800–829–4059** to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call **1–800–829–4477** to listen to pre-recorded messages covering various tax topics.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we evaluate the quality of our telephone services in several ways.

- A second IRS representative sometimes monitors live telephone calls. That person only evaluates the IRS assistor and does not keep a record of any taxpayer's name or tax identification number.
- We sometimes record telephone calls to evaluate IRS assistors objectively. We hold these recordings no longer than one week and use them only to measure the quality of assistance.
- We value our customers' opinions. Throughout this year, we will be surveying our customers for their opinions on our service.

Walk-in. You can walk in to many post offices, libraries, and IRS offices to pick up certain forms, instructions, and publications. Also, some libraries and IRS offices have:

- An extensive collection of products available to print from a CD-ROM or photocopy from reproducible proofs.
- The Internal Revenue Code, regulations, Internal Revenue Bulletins, and Cumulative Bulletins available for research purposes.

Mail. You can send your order for forms, instructions, and publications to the Distribution Center nearest to you and receive a response 7 to 15 workdays after your request is received. Find the address that applies to your part of the country.

- **Western part of U.S.:**
  Western Area Distribution Center
  Rancho Cordova, CA 95743–0001
- **Central part of U.S.:**
  Central Area Distribution Center
  P.O. Box 8903
  Bloomington, IL 61702–8903
- **Eastern part of U.S. and foreign addresses:**
  Eastern Area Distribution Center
  P.O. Box 85074
  Richmond, VA 23261–5074

CD-ROM. You can order IRS Publication 1796, *Federal Tax Products on CD-ROM,* and obtain:

- Current tax forms, instructions, and publications.
- Prior-year tax forms, instructions, and publications.
- Popular tax forms which may be filled in electronically, printed out for submission, and saved for recordkeeping.
- Internal Revenue Bulletins.

The CD-ROM can be purchased from National Technical Information Service (NTIS) by calling **1–877–233–6767** or on the Internet at **www.irs.ustreas. gov/cdorders.** The first release is available in mid-December and the final release is available in late January.

Glossary

The definitions in this glossary are the meanings of the terms as used in this publication. The same term used in another publication may have a slightly different meaning.

Amortization: A ratable deduction for the cost of certain intangible property over the period specified by law. Examples of costs that can be amortized are goodwill, agreement not to compete, and research and mining exploration costs.

Business assets: Property used in the conduct of a trade or business, such as business machinery and office furniture.

Capital assets: Generally, everything you own for personal purposes or investment is a capital asset. This includes your home, personal car, or stocks and bonds. It does not include inventory or depreciable property.

Capital expenses: These are costs that must be added to (increase the basis of) your business investments or your capital assets.

Capitalization: Adding costs, such as improvements, to the basis of assets.

Depletion: Yearly deduction allowed to recover your investment in minerals in place or standing timber. To take the deduction, you must have the right to income from the extraction and sale of the minerals or the cutting of the timber.

Depreciation: Ratable deduction allowed over a number of years to recover your basis in property that is used more than one year for business or income producing purposes.

Fair market value (FMV): FMV is the price at which property would change hands between a buyer and a seller, neither having to buy or sell, and both having reasonable knowledge of all necessary facts.

Going concern value: Going concern value is the additional value of a trade or business that attaches to property because the property is an integral part of a going concern. It includes value based on the ability of a business to continue to function and generate income even though there is a change in ownership.

Goodwill: Goodwill is the value of a trade or business based on expected continued customer patronage due to its name, reputation, or any other factor.

Intangible property: Property that cannot be perceived by the senses such as goodwill, patents, copyrights, etc.

Like-class property: Depreciable tangible personal properties within the same General Asset Class in Revenue Procedure 87–56 or Product Class in the *Standard Industrial Classification Manual.* See *Personal property* under *Like Property* in chapter 1 of Publication 544 for detailed information.

Like-kind property: Items of property with the same nature or character. The grade or quality of the properties does not matter. Examples are two vacant plots of land.

Nonbusiness assets: Property used for personal purposes, such as a home or family car.

Personal property: Property, such as machinery, equipment, or furniture, that is not real property.

Real property: Land and generally anything erected on, growing on, or attached to land, for example, a building.

Recapture: Amount of depreciation or section 179 deduction that must be reported as ordinary income when property is sold at a gain.

Section 179 deduction: This is a special deduction allowed against the cost of certain property purchased for use in the active conduct of a trade or business.

Section 197 intangibles: Certain intangibles held in connection with the conduct of a trade or business or an activity entered into for profit, including goodwill, going concern value, patents, copyrights, formulas, franchises, trademarks, and trade names.

Tangible property: This is property that can be seen or touched, such as furniture and buildings.

Unstated interest: The part of the sales price treated as interest when an installment contract provides for little or no interest.

Index

■