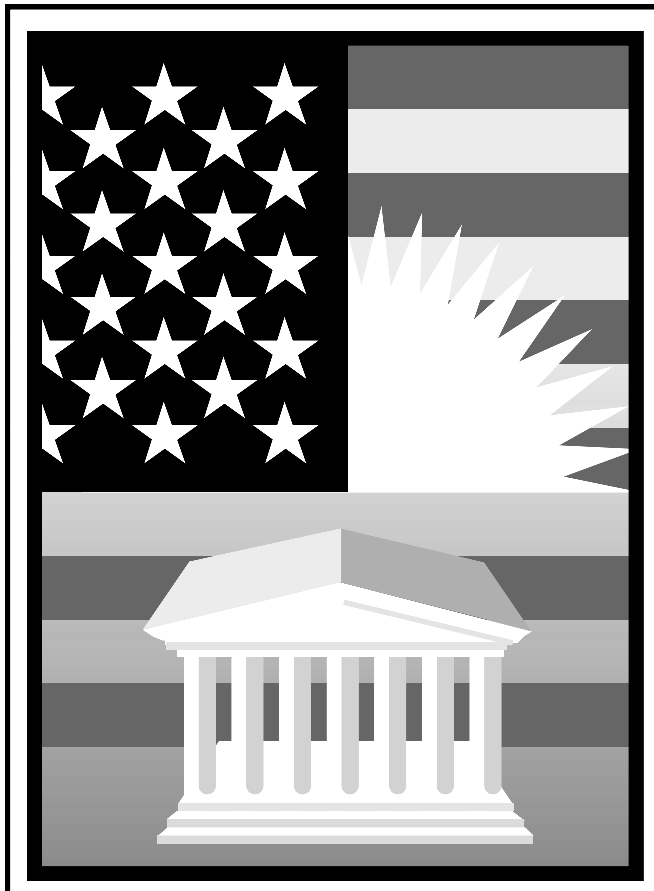
Department of the Treasury
Internal Revenue Service

Publication 523
Cat. No. 15044W

Selling Your Home

For use in preparing

1999 Returns



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.

Contents

Important Change for 1999 ... 1

Important Reminders ... 1

Introduction ... 2

Chapter 1. Main Home ... 2

Chapter 2. Rules for Sales in 1999 ... 3
- How To Figure Gain or Loss ... 3
- Choosing To Use Rules in Chapter 3 ... 4
- Gain on Sale ... 5
- Loss on Sale ... 5
- Basis ... 5
- Excluding the Gain ... 10
- Ownership and Use Tests ... 12
- Special Situations ... 15
- Reporting the Gain ... 16
- Real Estate and Transfer Taxes ... 19

Chapter 3. Rules Under Prior Law ... 19
- Postponing Gain ... 19
- How and When To Report ... 27
- One-Time Exclusion of Gain ... 29

Chapter 4. Recapture of Federal Subsidy ... 36

Chapter 5. How To Get More Information ... 36

Index ... 38

Important Change for 1999

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.

Important Reminders

Change of address. If you change your mailing address, be sure to notify the Internal Revenue Service (IRS) using Form 8822, *Change of Address.* Mail it to the Internal Revenue Service Center for your old address. (Addresses for the Service Centers are on the back of the form.)

Home sold with undeducted points. If you have not deducted all the points you paid to secure a mortgage on your old home, you may be able to deduct the remaining points in the year of sale. See *Points* in Part I of Publication 936, *Home Mortgage Interest Deduction.*

Introduction

This publication explains the tax rules that apply when you sell your main home. Generally, your main home is the one in which you live most of the time.

Gain. If you have a gain from the sale of your main home, you may be able to exclude it from income up to a limit of $250,000 ($500,000 on a joint return in most cases).

Loss. You cannot deduct a loss from the sale of your main home.

Worksheets. Worksheets are included in the publication to help you figure the adjusted basis of the home you sold, the gain (or loss) on the sale, and the amount of the gain that you can exclude.

Reporting the sale. Do not report the sale of your main home on your tax return unless you have a gain and at least part of it is taxable. Report any taxable gain on Schedule D (Form 1040).

Who may need to read chapter 3. Chapter 3 of this publication explains the rules that applied to sales before May 7, 1997. Those rules may still apply to you if you are in either of the following situations.

1) You sold your main home at a gain before May 7, 1997, and either:

   a) Bought a new home in 1999 within the replacement period, or

   b) Did not buy a new home before your replacement period ended in 1999.

2) You sold your main home at a gain in 1999 and made the choice described on page 4.

If you are in either of these situations and have questions, see chapter 3.

Date of sale. If you received a Form 1099–S, *Proceeds From Real Estate Transactions*, the date of sale should be shown in box 1. If you did not receive this form, the date of sale is the earlier of (a) the date title transferred or (b) the date economic burdens and benefits of ownership shifted to the buyer. In most cases, these dates are the same.

What is not covered in this publication. This publication does not cover the sale of rental property, second homes, or vacation homes. For information on how to report those sales, see Publication 544, *Sales and Other Dispositions of Assets.*

Useful Items

You may want to see:

Publication

- ☐ **521** Moving Expenses
- ☐ **527** Residential Rental Property
- ☐ **530** Tax Information for First-Time Homeowners
- ☐ **544** Sales and Other Dispositions of Assets
- ☐ **547** Casualties, Disasters, and Thefts (Business and Nonbusiness)
- ☐ **551** Basis of Assets
- ☐ **587** Business Use of Your Home
- ☐ **936** Home Mortgage Interest Deduction

Form (and Instructions)

- ☐ **Schedule D (Form 1040)** Capital Gains and Losses
- ☐ **1040X** Amended U.S. Individual Income Tax Return
- ☐ **8822** Change of Address
- ☐ **8828** Recapture of Federal Mortgage Subsidy

See chapter 5 for information about getting these publications and forms.

1.

Main Home

This chapter explains the term “main home.”

Usually, the home you live in most of the time is your main home and can be a:

- House,
- Houseboat,
- Mobile home,
- Cooperative apartment, or
- Condominium.

To exclude gain under the rules in chapter 2, you generally must have 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.

To postpone gain under the rules in chapter 3, the home you sold and the home you buy to replace it must both qualify as your main home.

Land. You may sell the land on which your main home is located, but not the house itself. In this case, you cannot postpone or exclude any gain you have from the sale of the land.

Example. On March 3, 1999, you sell the land on which your main home is located. You buy another piece of land and move your house to it. This sale is not considered a sale of your main home, and you cannot exclude any gain on the sale.

More than one home. If you have more than one home, only the sale of your main home qualifies for postponing or excluding gain. If you have two homes and live in both of them, your main home is ordinarily the one you live in most of the time.

Example 1. You own and live in a house in town. You also own a beach house, which you use in the summer months. The town house is your main home; the beach house is not.

Example 2. You own a house, but you live in another house that you rent. The rented home is your main home.

Property used partly as your home. If you use only part of the property as your main home, the rules discussed in this publication apply only to the gain or loss on the sale of that part of the property. For details, see *Business Use or Rental of Home* in chapter 2. Also see *Part of property used as main home* in chapter 3 under *Age, Ownership, and Use Tests for Sales Before May 7, 1997*.

2. Rules for Sales in 1999

Generally, you use the rules in this chapter if you sold your main home in 1999.

You may be able to exclude any gain from income up to a limit of $250,000 ($500,000 on a joint return in most cases). If you can exclude all of the gain, you do not need to report the sale on your tax return.

If you have gain that cannot be excluded, report it on Schedule D (Form 1040).

The main topics in this chapter are:

- How to figure gain or loss,
- Choosing to use rules in chapter 3,
- Gain on sale,
- Loss on sale,
- Basis,
- Excluding gain,
- Ownership and use tests,
- Special situations,
- Reporting gain, and
- Real estate and transfer taxes.

This chapter includes worksheets you can use to figure your gain (or loss) and your exclusion. Use Worksheet 1 to figure the adjusted basis of the home you sold. Use Worksheet 2 to figure the gain (or loss), the exclusion, and the taxable gain (if any) on the sale. If you cannot take the full exclusion, use Worksheet 3 to figure the reduced exclusion amount.

How To Figure Gain or Loss

To figure the gain or loss on the sale of your main home, you must know the **selling price**, the **amount realized**, and the **adjusted basis**.

Selling price. The selling price is the total amount you receive for your home. It includes money, all notes, mortgages, or other debts assumed by the buyer as part of the sale, and the fair market value of any other property or any services you receive.

Personal property. The selling price of your home does not include amounts you received for personal property sold with your home. Personal property is property that is not a permanent part of the home. Examples are furniture, draperies, and lawn equipment. Separately stated cash you received for these items should not be shown on Form 1099–S (discussed later).

Payment by employer. You may have to sell your home because of a job transfer. If your employer pays you for a loss on the sale or for your selling expenses, do ***not*** include the payment as part of the selling price. Your employer will include it in box 1 of your Form W–2 and you will include it in your gross income as wages on line 7 for Form 1040.

Option to buy. If you grant an option to buy your home and the option is exercised, add the amount you receive for the option to the selling price of your home. If the option is not exercised, you must report the amount as ordinary income in the year the option expires. Report this amount on line 21 of Form 1040.

Form 1099–S. If you received Form 1099–S, box 2 should show the total amount you received for your home.

However, box 2 will not include the fair market value of any property other than cash or notes, or any services, you received or will receive. Instead, box 4 will be checked.

If you can exclude the entire gain, the person responsible for closing the sale generally will not have to report it on Form 1099–S. You will use sale documents and other records to figure the total amount you received for your home.

Amount realized. The amount realized is the selling price minus selling expenses.

Selling expenses. Selling expenses include commissions, advertising fees, legal fees, and loan charges paid by the seller, such as loan placement fees or "points."

Adjusted basis. While you owned your home, you may have made adjustments (increases or decreases) to the basis. This adjusted basis is used to figure gain or loss on the sale of your home. For information on how to figure your home's adjusted basis, see *Basis,* later.

Amount of gain or loss. When you know the amount realized and the home's adjusted basis, you can figure your gain or loss. If the amount realized is more than the adjusted basis, the difference is a gain and, except for any part you can exclude, generally is taxable.

If the amount realized is less than the adjusted basis, the difference is a loss. A loss on the sale of your main home cannot be deducted.

Jointly owned home. If you and your spouse sell your jointly owned home and file a joint return, you figure your gain or loss as one taxpayer.

Separate returns. If you file separate returns, each of you must figure your own gain or loss according to your ownership interest in the home. Your ownership interest is determined by state law.

Joint owners not married. If you and a joint owner other than your spouse sell your jointly owned home, each of you must figure your own gain or loss according to your ownership interest in the home. Each of you applies the rules discussed in this publication on an individual basis.

Trading homes. If you trade your old home for another home, treat the trade as a sale and a purchase.

Example. You owned and lived in a home with an adjusted basis of $41,000. A real estate dealer accepted your old home as a trade-in and allowed you $50,000 toward a new house priced at $80,000. You are considered to have sold your old home for $50,000 and to have had a gain of $9,000 ($50,000 − $41,000).

If the dealer had allowed you $27,000 and assumed your unpaid mortgage of $23,000 on your old home, your sales price would still be $50,000 (the $27,000 trade-in allowed plus the $23,000 mortgage assumed).

Foreclosure or repossession. If your home was foreclosed on or repossessed, you have a sale.

You figure the gain or loss from the sale in generally the same way as gain or loss from any sale. But the amount of your gain or loss depends, in part, on whether you were personally liable for repaying the debt secured by the home, as shown in the following chart.

IF you were ...	THEN your selling price includes ...
Not personally liable for the debt	The full amount of debt canceled by the foreclosure or repossession.
Personally liable for the debt	The amount of canceled debt up to the home's fair market value. You may also have ordinary income, as explained next.

Ordinary income. If you were personally liable for the canceled debt, you may have ordinary income in addition to any gain or loss. If the canceled debt is more than the home's fair market value, you have ordinary income equal to the difference. Report that income on line 21, Form 1040. However, the income from cancellation of debt is not taxed to you if the cancellation is intended as a gift, or if you are insolvent or bankrupt. For more information on insolvency or bankruptcy, see Publication 908, *Bankruptcy Tax Guide*.

Form 1099–A and Form 1099–C. Generally, you will receive Form 1099–A, *Acquisition or Abandonment of Secured Property,* from your lender. This form will have the information you need to determine the amount of your gain or loss and whether you have any ordinary income from cancellation of debt. If your debt is canceled, you may receive Form 1099–C, *Cancellation of Debt*.

More information. If part of your home is used for business or rental purposes, see *Foreclosures and Repossessions* in chapter 1 of Publication 544 for more information. Publication 544 also has examples of how to figure gain or loss on a foreclosure or repossession.

Abandonment. If you abandon your home, you may have ordinary income. If the abandoned home secures a debt for which you are personally liable and the debt is canceled, you have ordinary income equal to the amount of canceled debt.

If the home is secured by a loan and the lender knows the home has been abandoned, the lender should send you Form 1099–A or Form 1099–C. See *Foreclosure or repossession*, earlier, for information about those forms. If the home is later foreclosed on or repossessed, gain or loss is figured as explained in that discussion.

Transfer to spouse. If you transfer your home to your spouse, or to your former spouse incident to your divorce, you generally have no gain or loss (unless the *Exception* applies). This is true even if you receive cash or other consideration for the home. Therefore, the rules explained in this publication do not apply.

If you owned your home jointly with your spouse and transfer your interest in the home to your spouse, or to your former spouse incident to your divorce, the same rule applies. You have no gain or loss.

A transfer of your home to your spouse, or to your former spouse incident to divorce, does not affect the basis of any new home you buy or build.

Exception. These transfer rules do not apply if your spouse or former spouse is a nonresident alien. In that case, you generally will have a gain or loss.

More information. See *Property Settlements* in Publication 504, *Divorced or Separated Individuals,* if you need more information.

Choosing To Use Rules in Chapter 3

Generally, you use the rules in chapter 2 if you sold your main home in 1999.

You can choose to use the rules in chapter 3, rather than the rules in this chapter, if you bought a new home on or before August 5, 1997, (or under a binding contract that was in effect on that date) and sold your old home within 2 years after buying the new home.

Example. You sold your old main home at a gain on February 3, 1999. On June 27, 1997, before selling your old main home, you bought and moved into a new one. You can choose whether to use the rules of this chapter or the rules of chapter 3.

Sales before 1999. You were also eligible to make this choice if:

- You sold your home after May 6, 1997, and before August 6, 1997, or
- You sold your home under a contract that was binding on August 5, 1997.

TIP *You might want to use the rules in chapter 3 if you cannot exclude your entire gain under the rules in this chapter. In that case, compare the amount of gain that would be taxed using the rules in this chapter with the amount that would be taxed using the rules in chapter 3.*

Gain on Sale

You will generally be subject to tax on all of the gain on the sale of your main home unless you exclude all or part of the gain under the rules described in this chapter.

Loss on Sale

You ***cannot*** deduct a loss on the sale of your home. It is a personal loss.

Payment by employer. You must include in income any amount your employer pays you for a loss on the sale of your home or for expenses of the sale when you transfer to a new location. Do **not** include the payment as part of the selling price. Your employer will include it with the rest of your wages in box 1 of your Form W–2 and you will include it in your gross income as wages on line 7 of Form 1040.

Basis

You will need to know your basis in your home as a starting point for determining any gain or loss when you sell it. Your basis in your home is determined by how you got the home. Your basis is its cost if you bought it or built it. If you got it in some other way, its basis is either its fair market value when you received it or the adjusted basis of the person you received it from.

While you owned your home, you may have made adjustments (increases or decreases) to the basis. This ***adjusted basis*** is used to figure gain or loss on the sale of your home.

To figure your adjusted basis, you can use Worksheet 1. A filled-in example of that worksheet is included in the comprehensive *Illustrated Example* later in this chapter.

Table 1 in this publication explains how to use the worksheet in certain special situations.

The main topics in this section are:

- Cost as basis,
- Basis other than cost, and
- Adjusted basis.

Cost As Basis

The cost of property is the amount you pay for it in cash, debt obligations, or other property.

Purchase. If you buy your home, your basis is its cost to you. This includes the purchase price and certain settlement or closing costs. Your purchase price includes your down payment and any debt, such as a first or second mortgage or notes you gave the seller in payment for the home.

Seller-paid points. If the person who sold you your home paid points on your loan, you may have to reduce your home's basis by the amount of the points, as shown in the chart below.

IF you bought your home ...	THEN reduce your home's basis by the seller-paid points ...
After 1990 but before April 4, 1994	Only if you chose to deduct them as home mortgage interest in the year paid.
After April 3, 1994	Even if you did not deduct them.

If you must reduce your basis by seller-paid points and you use Worksheet 1 to figure your adjusted basis, enter the seller-paid points on line 2 of the worksheet (unless you used the seller-paid points to reduce the amount on line 1).

Settlement fees or closing costs. When buying your home, you may have to pay settlement fees or closing costs in addition to the contract price of the property. You can include in your basis the settlement fees and closing costs you pay for buying the home. You cannot include in your basis the fees and costs for getting a mortgage loan. A fee for buying the home is any fee you would have had to pay even if you paid cash for the home.

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

Some of the settlement fees or closing costs that you can include in the basis of your property are:

1) Abstract fees (abstract of title fees),
2) Charges for installing utility services,
3) Legal fees (including fees for the title search and preparing the sales contract and deed),
4) Recording fees,
5) Survey fees,

6) Transfer taxes,

7) Owner's title insurance, and

8) Any amounts the seller owes that you agree to pay, such as:

   a) Certain real estate taxes (discussed in detail later),

   b) Back interest,

   c) Recording or mortgage fees,

   d) Charges for improvements or repairs, and

   e) Sales commissions.

Some settlement fees and closing costs ***not*** included in your basis are:

1) Fire insurance premiums,

2) Rent for occupancy of the house before closing,

3) Charges for utilities or other services related to occupancy of the house before closing,

4) Any fee or cost that you deducted as a moving expense (allowed for certain fees and costs before 1994),

5) Charges connected with getting a mortgage loan, such as:

   a) Mortgage insurance premiums (including VA funding fees),

   b) Loan assumption fees,

   c) Cost of a credit report, and

   d) Fee for an appraisal required by a lender, and

6) Fees for refinancing a mortgage.

See *Settlement fees or closing costs* under *How To Figure Cost of New Home* in chapter 3 for information about the fees and costs (real estate taxes and mortgage interest, including points) that you may be able to deduct.

Real estate taxes. Real estate taxes for the year you bought your home may affect your basis, as shown in the following chart.

IF ...	AND ...	THEN the taxes ...
You pay taxes that the seller owed on the home (the taxes up to the date of the sale)	The seller does *not* reimburse you	Are added to the basis of your home.
	The seller reimburses you	Do *not* affect the basis of your home.
The seller paid taxes for you (the taxes beginning on the date of sale)	You do *not* reimburse the seller	Are subtracted from the basis of your home.
	You reimburse the seller	Do *not* affect the basis of your home.

Construction. If you contracted to have your house built on land you own, your basis is:

1) The cost of the land, plus

2) The amount it cost you to complete the house, including:

   a) The cost of labor and materials,

   b) Any amounts paid to a contractor,

   c) Any architect's fees,

   d) Building permit charges,

   e) Utility meter and connection charges, and

   f) Legal fees directly connected with building the house.

Your cost includes your down payment and any debt, such as a first or second mortgage or notes you gave the seller or builder. It also includes certain settlement or closing costs. You may have to reduce the basis by points the seller paid for you. For more information, see *Seller-paid points* and *Settlement fees or closing costs,* earlier.

Built by you. If you built all or part of your house yourself, its basis is the total amount it cost you to complete it. Do not include in the cost of the house:

- The value of your own labor, or
- The value of any other labor you did not pay for.

Temporary housing. If a builder gave you temporary housing while your home was being finished, you must reduce your basis by the part of the contract price that applies to temporary housing. To figure the amount of the reduction, use the method described in *Temporary housing* under *How To Figure Cost of New Home* in chapter 3.

Cooperative apartment. Your basis in the apartment is usually the cost of your stock in the co-op housing corporation, which may include your share of a mortgage on the apartment building.

Condominium. Your basis is generally its cost to you.

Basis Other Than Cost

You must use a basis other than cost, such as fair market value, if you got your home as a gift, from your spouse, as an inheritance, or in a trade. If you got your home in any of these ways, see the following discussion that applies to you. If you want to figure your adjusted basis using Worksheet 1, see *Table 1* for help.

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

Home received as gift. Use the following chart to find the basis of a home you received as a gift.

IF the donor's adjusted basis at the time of the gift was ...	THEN your basis is ...
More than the fair market value of the home at that time	The same as the donor's adjusted basis at the time of the gift. *Exception:* If using the donor's adjusted basis results in a loss when you sell the home, you must use as your basis the fair market value of the home at the time of the gift. *Neither gain nor loss:* If using the fair market value results in a gain, you have neither gain nor loss.
Equal to or less than the fair market value at that time, and you received the gift before 1977	The smaller of the: • Donor's adjusted basis, plus any federal gift tax paid on the gift, or • The home's fair market value at the time of the gift.
Equal to or less than the fair market value at that time, and you received the gift after 1976	The same as the donor's adjusted basis, plus the part of any federal gift tax paid that is due to the net increase in value of the home (explained next).

Part of federal gift tax due to net increase in value. Figure the part of the federal gift tax paid that is due to the net increase in value of the home by multiplying the total federal gift tax paid by a fraction. The numerator (top part) of the fraction is the net increase in the value of the home, and the denominator (bottom part) is the fair market value of the home. The net increase in the value of the home is its fair market value minus the donor's adjusted basis.

Home received from spouse. You may have received your home from your spouse or from your former spouse incident to your divorce.

Transfers after July 18, 1984. If you received the home after July 18, 1984, you had no gain or loss on the transfer. Your basis in this home is generally the same as your spouse's (or former spouse's) adjusted basis just before you received it. This rule applies even if you received the home in exchange for cash, the release of marital rights, the assumption of liabilities, or other consideration.

If you owned a home jointly with your spouse and your spouse transferred his or her interest in the home to you, your basis in the half interest received from your spouse is generally the same as your spouse's adjusted basis just before the transfer. This also applies if your former spouse transferred his or her interest in the home to you incident to your divorce. Your basis in the half interest you already owned does not change. Your new basis in the home is the total of these two amounts.

Transfers before July 19, 1984. If you received your home before July 19, 1984, in exchange for your release of marital rights, your basis in the home is generally its fair market value at the time you received it.

More information. For more information on property received from a spouse or former spouse, see *Property Settlements* in Publication 504.

Home received as inheritance. If you inherited your home, its basis is its fair market value on the date of the decedent's death or the later alternate valuation date if that date was used for federal estate tax purposes. If an estate tax return was filed, the value listed there for the property generally is your basis. If a federal estate tax return did not have to be filed, your basis in the home is the same as its appraised value at the date of death for purposes of state inheritance or transmission taxes.

Surviving spouse. If you are a surviving spouse and you owned your home jointly, your basis in the home will change. The new basis for the half interest that your spouse owned will be one-half of the fair market value on the date of death (or alternate valuation date). The basis in your half will remain one-half of the adjusted basis determined previously. Your new basis is the total of these two amounts.

Example. Your jointly owned home had an adjusted basis of $50,000 on the date of your spouse's death, and the fair market value on that date was $100,000. Your new basis in the home is $75,000 ($25,000 for one-half of the adjusted basis plus $50,000 for one-half of the fair market value).

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

For more information about community property, see Publication 555, *Community Property.*

Home received in trade. If you acquired your home in a trade for other property, the basis of your home is generally the fair market value of the other property at the time of the trade. If you traded one home for another, you have made a sale and purchase. In that case, you may have realized a gain. See *Trading homes,* earlier, for an example of figuring the gain.

More information. For more information about basis, get Publication 551.

Adjusted Basis

Adjusted basis is your basis ***increased*** or ***decreased*** by certain amounts.

To figure your adjusted basis, you can use Worksheet 1. A filled-in example of that worksheet is included in a comprehensive *Illustrated Example* later in this chapter. *Table 1* explains how to use the worksheet in certain special situations.

Increases to basis. These include any:

1) Improvements that have a useful life of more than 1 year,
2) Additions,
3) Special assessments for local improvements, and
4) Amounts you spent after a casualty to restore damaged property.

Decreases to basis. These include any:

1) Gain you postponed from the sale of a previous home before May 7, 1997,
2) Deductible casualty losses,
3) Insurance payments you received or expect to receive for casualty losses,
4) Payments you received for granting an easement or right-of-way,
5) Depreciation allowed or allowable if you used your home for business or rental purposes,
6) Residential energy credit (generally allowed from 1977 through 1987) claimed for the cost of energy improvements that you added to the basis of your home,
7) Adoption credit you claimed for improvements that you added to the basis of your home,
8) Nontaxable payments from an adoption assistance program of your employer that you used for improvements you added to the basis of your home,
9) First-time homebuyers credit (allowed to certain first-time buyers of a home in the District of Columbia), and
10) Energy conservation subsidy excluded from your gross income because you received it (directly or indirectly) from a public utility after 1992 to buy or install any energy conservation measure. An energy conservation measure is an installation or modification that is primarily designed either to reduce consumption of electricity or natural gas or to improve the management of energy demand for a home.

Improvements. These add to the value of your home, prolong its useful life, or adapt it to new uses. You add the cost of improvements to the basis of your property.

Examples. Putting a recreation room in your unfinished basement, adding another bathroom or bedroom, putting up a new fence, putting in new plumbing or wiring, putting on a new roof, or paving your unpaved driveway are improvements.

The chart below lists some other examples of improvements.

Additions Bedroom Bathroom Deck Garage Porch Patio **Lawn & Grounds** Landscaping Driveway Walkway Fence Retaining wall Sprinkler system Swimming pool **Miscellaneous** Storm windows, doors New roof Central vacuum Wiring upgrades Satellite dish Security system	**Heating & Air Conditioning** Heating system Central air conditioning Furnace Duct work Central humidifier Filtration system **Plumbing** Septic system Water heater Soft water system Filtration system **Interior Improvements** Built-in appliances Kitchen modernization Flooring Wall-to-wall carpeting **Insulation** Attic Walls, floor Pipes, duct work

Improvements no longer part of home. Your home's adjusted basis does not include the cost of any improvements that are no longer part of the home.

Example. You put wall-to-wall carpeting in your home 15 years ago. Later, you replaced that carpeting with new wall-to-wall carpeting. The cost of the old carpeting you replaced is no longer part of your home's adjusted basis.

Repairs. These maintain your home in good condition but do not add to its value or prolong its life. You do not add their cost to the basis of your property.

Examples. Repainting your house inside or outside, fixing your gutters or floors, repairing leaks or plastering, and replacing broken window panes are examples of repairs.

Exception. The entire job is considered an improvement, however, if items that would otherwise be considered repairs are done as part of an extensive remodeling or restoration of your home.

Recordkeeping. You should keep records to prove your home's adjusted basis. Ordinarily, you must keep records for 3 years after the due date for filing your return for the tax year in which you sold your home. But if the basis of your old home affects the basis of your new one, such as when you sold your

Table 1. **How To Use Worksheet 1 in Special Situations**

If you use Worksheet 1, *Adjusted Basis of Home Sold,* and any of the situations described below apply to you, follow these instructions.

IF...		**Then...**
You inherited your home	1	Skip lines 1–4 of the worksheet.
	2	Find your basis using the rules under *Home received as inheritance* in this publication. Enter this amount on line 5 of the worksheet.
	3	Fill out the rest of the worksheet.
You received your home as a gift	1	Read *Home received as gift* in this publication and enter on line 1 and 3 of the worksheet either the donor's adjusted basis or the home's fair market value at the time of the gift, whichever is appropriate.
	2	If you can add any federal gift tax to your basis, enter that amount on line 5 of the worksheet.
	3	Fill out the rest of the worksheet.
You received your home in a trade	1	Find your basis using the rules under *Home received in trade* in this publication. Enter this amount on line 1 of the worksheet. (But if you received your home in a trade for your previous home before May 7, 1997,* and had a gain on the trade that you postponed using a Form 2119, enter on line 1 of the worksheet the adjusted basis of the new home from that Form 2119.)
	2	Fill out the rest of the worksheet.
You built your home	1	Add the purchase price of the land and the cost of building the home (see *Construction* in this publication for details). Enter that total on line 1 of the worksheet. (However, if you filed a Form 2119 to postpone gain on the sale of a previous home before May 7, 1997,* enter on line 1 of the worksheet the adjusted basis of the new home from that Form 2119.)
	2	Fill out the rest of the worksheet.
You received your home from your spouse after July 18, 1984	1	Skip lines 1–4 of the worksheet.
	2	Enter on line 5 of the worksheet your spouse's adjusted basis in the home just before you received it.
	3	Fill out the rest of the worksheet, making adjustments to basis only for events after the transfer.
You owned a home jointly with your spouse, who transferred his or her interest in the home to you after July 18, 1984		Fill out one worksheet, including adjustments to basis for events both before and after the transfer.
You received your home from your spouse before July 19, 1984	1	Skip lines 1–4 of the worksheet.
	2	Enter on line 5 of the worksheet the home's fair market value at the time you received it.
	3	Fill out the rest of the worksheet, making adjustments to basis only for events after the transfer.
You owned a home jointly with your spouse, and your spouse transferred his or her interest in the home to you before July 19, 1984	1	Fill out a worksheet, lines 1–13, making adjustments to basis only for events before the transfer.
	2	Multiply the amount on line 13 of that worksheet by one-half (0.5) to get the adjusted basis of your half interest at the time of the transfer.
	3	Multiply the fair market value of the home at the time of the transfer by one-half (0.5). Generally, this is the basis of the half interest that your spouse owned.
	4	Add the amounts from steps 2 and 3 and enter the total on line 5 of a second worksheet.
	5	Complete the rest of the second worksheet, making adjustments to basis only for events after the transfer.

Table 1 *(Continued)*

You owned your home jointly with your spouse who died	1	Fill out a worksheet, lines 1–13, making adjustments to basis only for events before your spouse's death.
	2	Multiply the amount on line 13 of the worksheet by one-half (0.5) to get the adjusted basis of your half interest on the date of death.
	3	Use the rules under *Surviving spouse* in this publication to find the basis for the half interest that was owned by your spouse.
	4	Add the amounts from steps 2 and 3 and enter the total on line 5 of a second worksheet.
	5	Complete the rest of the second worksheet, making adjustments to basis only for events after your spouse's death.
You owned your home jointly with your spouse who died, and your permanent home is in a community property state	1	Skip lines 1–4 of the worksheet.
	2	Enter the amount of your basis on line 5 of the worksheet. Generally, this is the fair market value of the home at the time of death. (But see *Community property* in this publication.)
	3	Fill out the rest of the worksheet, making adjustments to basis only for events after your spouse's death.
Your home was ever damaged as a result of a casualty	1	On line 8 of the worksheet, enter any amounts you spent to restore the home to its condition before the casualty.
	2	On line 11 enter: Any insurance reimbursements you received (or expect to receive) for the loss, and Any deductible casualty losses not covered by insurance.

*Includes certain sales after May 6, 1997, for which you made the choice described on page 4.

old home before May 7, 1997, and postponed tax on any gain, you should keep those records as long as they are needed for tax purposes.

The records you should keep include:

- Proof of the home's purchase price and purchase expenses,
- Receipts and other records for all improvements, additions, and other items that affect the home's adjusted basis,
- Any worksheets you used to figure the adjusted basis of the home you sold, the gain or loss on the sale, the exclusion, and the taxable gain,
- Any Form 2119 that you filed to postpone gain from the sale of a previous home before May 7, 1997, and
- Any worksheets you used to prepare Form 2119, such as the *Adjusted Basis of Home Sold Worksheet* or the *Capital Improvements Worksheet* from the Form 2119 instructions.

Excluding the Gain

You may qualify to exclude from your income all or part of any gain from the sale of your main home. This means that, if you qualify, you will not have to pay tax on the gain up to the limit described under *Maximum Amount of Exclusion*, next. To qualify, you must meet the ownership and use tests described later.

You can choose not to take the exclusion. In that case, you will have to pay tax on your entire gain, unless you make the choice described on page 4.

You can use Worksheet 2 on page 11 to figure the amount of your exclusion and your taxable gain, if any.

Maximum Amount of Exclusion

You can exclude the entire gain on the sale of your main home up to:

1) $250,000, or

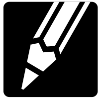
2) $500,000 if all of the following are true.

   a) You are married and file a joint return for the year.

   b) Either you or your spouse meets the ownership test.

   c) Both you and your spouse meet the use test.

   d) During the 2-year period ending on the date of the sale, neither you nor your spouse excluded



Worksheet 1. **Adjusted Basis of Home Sold**

Caution: *See if any of the situations listed in Table 1 apply to you before you use this worksheet.*

1.	Enter the purchase price of your old home. If you filed Form 2119 when you originally acquired your old home to postpone gain on the sale of a previous home, enter the adjusted basis of the new home from that Form 2119	**1.** ______
2.	Seller-paid points, for home bought after 1990. (See *Seller-paid points* in this chapter.) Do not include any seller-paid points you previously subtracted to arrive at the amount entered on line 1, above	**2.** ______
3.	Subtract line 2 from line 1	**3.** ______
4.	Settlement fees or closing costs. See *Settlement fees or closing costs* in this chapter. If line 1 includes the adjusted basis of the new home from Form 2119, go to line 6.	
a.	Abstract and recording fees **a.** ______	
b.	Legal fees (including title search and preparing document) **b.** ______	
c.	Surveys **c.** ______	
d.	Title insurance **d.** ______	
e.	Transfer or stamp taxes **e.** ______	
f.	Amounts the seller owed that you agreed to pay (back taxes or interest, recording or mortgage fees, and sales commissions) **f.** ______	
g.	Other **g.** ______	
5.	Add lines 4a through 4g	**5.** ______
6.	Cost of capital improvements. Do not include any capital improvements included on line 1 above	**6.** ______
7.	Special tax assessments paid on your old home for local improvements, such as streets and sidewalks	**7.** ______
8.	Other increases to basis	**8.** ______
9.	Add lines 3, 5, 6, 7, and 8	**9.** ______
10.	Depreciation, related to the business use or rental of your old home, claimed (or allowable) **10.** ______	
11.	Other decreases to basis (see *Decreases to basis* in this chapter.) **11.** ______	
12.	Add lines 10 and 11	**12.** ______
13.	**ADJUSTED BASIS OF HOME SOLD.** Subtract line 12 from line 9. Enter here and on Worksheet 2, line 4	**13.** ______

Worksheet 2. **Gain (or Loss), Exclusion, and Taxable Gain**

Part 1–Gain (or Loss) on Sale

1.	Selling price of home	**1.** ______
2.	Selling expenses	**2.** ______
3.	Subtract line 2 from line 1	**3.** ______
4.	Adjusted basis of home sold. (From Worksheet 1, line 13.)	**4.** ______
5.	Subtract line 4 from line 3. This is the **gain** (**or loss**) on the sale. If this is a loss, stop here	**5.** ______

Part 2–Exclusion and Taxable Gain

6.	Enter any depreciation claimed on the property for periods after May 6, 1997. If none, enter zero	**6.** ______
7.	Subtract line 6 from line 5. (If the result is less than zero, enter zero.)	**7.** ______
8.	If you qualify to exclude gain on the sale, enter your maximum exclusion. (See *Maximum Amount of Exclusion* in this chapter.) If you do not qualify to exclude gain, enter -0-	**8.** ______
9.	Enter the smaller of line 7 or line 8. This is your exclusion	**9.** ______
10.	Subtract line 9 from line 5. This is your taxable gain. Report it as described under *Reporting the Gain* on page 16. If the amount on this line is zero, do not report the sale or exclusion on your tax return. **If the amount on line 6 is more than zero, complete line 11**	**10.** ______
11.	Enter the smaller of line 6 or line 10. Enter this amount on line 10 of the *Unrecaptured Section 1250 Gain Worksheet* in the instructions for Schedule D (Form 1040)	**11.** ______

gain from the sale of another home (not counting any sales before May 7, 1997).

Reduced Maximum Exclusion

You can claim an exclusion, but the maximum amount of gain you can exclude will be reduced, if any of the following are true.

1) You did not meet the ownership and use tests for a home you owned on August 5, 1997, and sold before August 5, 1999.

2) You did not meet the ownership and use tests for a home you sold due to a change in health or place of employment.

3) Your exclusion would have been disallowed because of the rule described in *More Than One Home Sold During 2-Year Period*, next, except that you sold the home due to a change in health or place of employment.

Use Worksheet 3 on page 13 to figure your reduced maximum exclusion.

More Than One Home Sold During 2-Year Period

You cannot exclude gain on the sale of your home if, during the 2-year period ending on the date of the sale, you sold another home at a gain and excluded all or part of that gain. If you cannot exclude the gain, you must include it in your income.

However, if you sold the home due to a change in health or place of employment, you can still claim an exclusion. The maximum amount you can exclude is reduced. See *Reduced Maximum Exclusion,* earlier.

Sales before May 7, 1997. When counting the number of sales during a 2-year period, do not count sales before May 7, 1997.

Example 1. In September 1997, Paul and Nadine bought a new home. In November 1997, they sold their old home at a $40,000 gain. They had owned and lived in the home for 4 years. They excluded the gain on the sale.

On October 1, 1999, Paul and Nadine sold the home they purchased in September 1997 at a $15,000 gain. The sale was not due to a change in health or place of employment. Because Paul and Nadine had excluded gain on the sale of another home within the 2-year period ending on October 1, 1999, they cannot exclude the gain on this sale.

Example 2. The facts are the same as in *Example 1* except that Paul and Nadine did not sell the home purchased in September 1997 until December 1, 1999. Because they had not excluded gain on the sale of another home within the 2-year period ending on December 1, 1999, they can exclude the gain on this sale.

Ownership and Use Tests

To claim the exclusion, you must meet the ownership and use tests. This means that during the ***5-year period*** ending on the date of the sale, you must have:

1) ***Owned*** the home for at least ***2 years*** (the ownership test), ***and***

2) ***Lived in*** the home as your main home for at least ***2 years*** (the use test).

Exception. If you owned and lived in the property as your main home for less than 2 years, you may still be able to claim an exclusion in some cases. The maximum amount you can exclude will be reduced. See *Reduced Maximum Exclusion,* earlier.

Period of ownership and use. The required 2 years of ownership and use (during the 5-year period ending on the date of the sale) do not have to be continuous. You meet the tests if you can show that you owned and lived in the property as your main home for either 24 full months or 730 days (365 × 2) during the 5-year period. Short temporary absences for vacations or other seasonal absences, even if you rent out the property during the absences, are counted as periods of use. See *Ownership and use tests met at different times,* later.

Example 1 — met use test but not ownership test. From 1990 through August 1998 Amanda lived with her parents in a house that her parents owned. On September 2, 1998, she bought this house from her parents. She continued to live there until December 15, 1999, when she sold it at a gain. Although Amanda ***lived in*** the property as her main home for more than 2 years, she did not ***own*** it for the required 2 years. She cannot exclude any part of her gain on the sale, unless she sold the property due to a change in health or place of employment, as explained under *Reduced Maximum Exclusion,* earlier.

Example 2 — period of absence. Professor Paul Beard, who is single, bought and moved into a house on August 30, 1996. He lived in it as his main home continuously until January 5, 1998, when he went abroad for a 1-year sabbatical leave. During part of the period of leave, the house was unoccupied, and during the rest of the period, he rented it out. On January 5, 1999, he sold the house. Because his leave was not a short temporary absence, he cannot include the period of leave to meet the 2-year use test. However, even though he did not live in the house for the required 2-year period, he does qualify for an exclusion because he owned the home on August 5, 1997, and sold it before August 5, 1999. See *Reduced Maximum Exclusion,* earlier. The maximum amount of gain he can exclude will be less than $250,000. In addition, he cannot exclude the part of the gain equal to the depreciation he claimed. See *Depreciation for business use after May 6, 1997*, later.

Worksheet 3. **Reduced Maximum Exclusion**

Caution: *Complete this worksheet only if you qualify for a reduced exclusion.* (See *Reduced Maximum Exclusion* in this chapter.) *Complete column (B) only if you are married filing a joint return.*

			(A) You	(B) Your Spouse
1.	Maximum amount	**1.**	$250,000.00	$250,000.00
2a.	Enter the number of days that you used the property as a main home during the 5-year period ending on the date of sale. (If married filing jointly, fill in columns (A) and (B))	**2a.**		
b.	Enter the number of days that you owned the property during the 5-year period ending on the date of sale. (If married filing jointly and one spouse owned the property longer than the other spouse, both spouses are treated as owning the property for the longer period)	**b.**		
c.	Enter the smaller of line 2a or 2b	**c.**		
3.	Have you (or your spouse if filing jointly) excluded gain from the sale of another home during the 2-year period ending on the date of this sale (not counting any sales before May 7, 1997)? **NO.** Skip line 3 and enter the number of days from line 2c on line 4. **YES.** Enter the number of days between the date of the most recent sale of another home on which you excluded gain and the date of sale of this home	**3.**		
4.	Enter the smaller of line 2c or 3	**4.**		
5.	Divide the amount on line 4 by 730 days. Enter the result as a decimal (rounded to at least 3 places). But do not enter an amount greater than 1.000	**5.**		
6.	Multiply the amount on line 1 by the decimal amount on line 5	**6.**		
7.	Add the amounts in column (A) and (B) of line 6. This is your reduced maximum exclusion. Enter it here and on Worksheet 2, line 8	**7.**		

Ownership and use tests met at different times. You can meet the ownership and use tests during different 2-year periods. However, you must meet both tests during the 5-year period ending on the date of the sale.

Example. In 1990, Helen Jones lived in a rented apartment. The apartment building was later changed to a condominium, and she bought her apartment on December 1, 1996. In 1997, Helen became ill and on April 14 of that year she moved to her daughter's home. On July 10, 1999, while still living in her daughter's home, she sold her apartment.

Helen can exclude gain on the sale of her apartment because she met the ownership and use tests. Her 5-year period is from July 11, 1994, to July 10, 1999, the date she sold the apartment. She owned her apartment from December 1, 1996, to July 10, 1999 (over 2 years). She lived in the apartment from July 11, 1994 (the beginning of the 5-year period), to April 14, 1997 (over 2 years).

Cooperative apartment. If you sold stock in a cooperative housing corporation, the ownership and use tests are that, during the 5-year period ending on the date of sale, you must have:

1) Owned the stock for at least 2 years, and

2) Lived in the house or apartment that the stock entitles you to occupy as your main home for at least 2 years.

Exception for individuals with a disability. There is an exception to the use test if, during the 5-year period before the sale of your home:

1) You become physically or mentally unable to care for yourself, and

2) You owned and lived in your home as your main home for a total of at least 1 year.

Under this exception, you are considered to live in your home during any time that you own the home and live in a facility (including a nursing home) that is licensed by a state or political subdivision to care for persons in your condition.

If you meet this exception to the use test, you still have to meet the 2-out-of-5-year ownership test to claim the exclusion.

Gain postponed on sale of previous home. For the ownership and use tests, you may be able to add the time you owned and lived in a previous home to the time you lived in the home on which you wish to exclude gain. You can do this if you postponed all or part of the gain on the sale of the previous home (as described under *Postponing Gain* in chapter 3) because of buying the home on which you wish to exclude gain.

In addition, if buying the previous home enabled you to postpone all or part of the gain on the sale of a home you owned earlier, you can also include the time you owned and lived in that earlier home.

Previous home destroyed or condemned. For the ownership and use tests, you add the time you owned and lived in a previous home that was destroyed or condemned to the time you owned and lived in the home on which you wish to exclude gain. This rule applies if any part of the basis of the home you sold depended on the basis of the destroyed or condemned home. Otherwise, you must have owned and lived in the ***same*** home for 2 of the 5 years before the sale to qualify for the exclusion.

Married Persons

If you and your spouse file a joint return for the year of sale, you can exclude gain if either spouse meets the ownership and use tests. (But see *Maximum Amount of Exclusion,* earlier.)

Example 1 — one spouse sells a home. Emily sells her home in June 1999. She marries Jamie later in the year. She meets the ownership and use tests, but Jamie does not. Emily can exclude up to $250,000 of gain on a separate or joint return for 1999.

Example 2 — each spouse sells a home. The facts are the same as in *Example 1* except that Jamie also sells a home. He meets the ownership and use tests on his home. Emily and Jamie can each exclude up to $250,000 of gain.

Death of spouse before sale. If your spouse died before the date of sale, you are considered to have owned and lived in the property as your main home during any period of time when your spouse owned and lived in it as a main home.

Home transferred from spouse. If your home was transferred to you by your spouse (or former spouse if the transfer was incident to divorce), you are considered to have owned it during any period of time when your spouse owned it.

Use of home after divorce. You are considered to have used property as your main home during any period when:

1) You owned it, and

2) Your spouse or former spouse is allowed to live in it under a divorce or separation instrument.

Business Use or Rental of Home

You may be able to exclude your gain from the sale of a home that you have used for business or to produce rental income. But you must meet the ownership and use tests.

Example. On May 30, 1993, Amy bought a house. She moved in on that date and lived in it until May 31, 1995, when she moved out of the house and put it up for rent. The house was rented from July 1, 1995, to March 31, 1997. Amy moved back into the house on April 1, 1997, and lived there until she sold it on January 31, 1999. During the 5-year period ending on the date of the sale (February 1, 1994 – January 31, 1999), Amy owned and lived in the house for more than 2 years as shown in the table below.

Five Year Period	Used as Home	Used as Rental
2/1/94 – 5/31/95	16 months	
6/1/95 – 3/31/97		22 months
4/1/97 – 1/31/99	22 months	
	38 months	22 months

Amy can exclude gain up to $250,000.

Depreciation for business use after May 6, 1997. If you were entitled to take depreciation deductions because you used your home for business purposes or as rental property, you cannot exclude the part of your gain equal to any depreciation allowed or allowable as a deduction for periods after May 6, 1997. If you can show by adequate records or other evidence that the depreciation deduction allowed was less than the amount allowable, the amount you cannot exclude is the smaller figure.

Example. Micah sold his main home in 1999 at a $30,000 gain. He meets the use and ownership tests to exclude the gain from his income. However, he used part of the home for business in 1998 and claimed $500 depreciation. He can exclude $29,500 ($30,000 – $500) of his gain. He has a taxable gain of $500.

Property used partly as your home and partly for business or rental during the year of sale. In the year of sale you may have used part of your property as your home and part of it for business or to produce income. Examples are:

- A working farm on which your house was located,
- An apartment building in which you lived in one unit and rented out the others,
- A store building with an upstairs apartment in which you lived, or
- A home with a room used for business or to produce income.

If you sell the entire property, you should consider the transaction as the sale of two properties. The sale of the part of your property used for business or rental is reported on Form 4797, *Sales of Business Property*.

To determine the amounts to report on Form 4797, you must divide your selling price, selling expenses, and basis between the part of the property used for business or rental and the part used as your home. In the same way, if you qualify to exclude any of the gain on the business or rental part of your home, also divide your maximum exclusion between that part of the property and the part used as your home. If you want to use Worksheet 2 to figure your exclusion and taxable gain from each part, fill out a separate Worksheet 2 (Part 2) for each.

Excluding gain on the business or rental part of your home. You generally can exclude gain on the part of your home used for business or rental **if** you owned and lived in that part of the home for at least 2 years during the 5-year period ending on the date of the sale. Enter the exclusion for the business or rental part on Form 4797 as explained in the Form 4797 instructions. If you used a separate Worksheet 2 (Part 2) to figure the exclusion for the business or rental part, fill it out only through line 9. Do not fill out lines 10 and 11 of that Worksheet 2.

Example. You sold your home on December 1, 1999. You had owned and lived in the home during the entire 5-year period ending on the date of sale. For the first 2½ years of that period, you used the entire house as your main home. For the last 2½ years, you used ¾ (75%) of the house as your main home and ¼ (25%) of the house for business. Your records show:

Purchase price	$80,000
Depreciation (on business part; all after 5/7/1997)	1,363
Selling price	160,000
Selling expenses	10,000

Because you meet the ownership and use tests for the entire house, you can claim the exclusion for both the home and business parts. You start by finding the adjusted basis of each part. You determine that three-fourths (75%) of your purchase price was for the part used as your home; one-fourth (25%) was for the part used for business.

	Personal (3/4)	Business (1/4)
Purchase price	$60,000	$20,000
Minus: Depreciation	–0–	1,363
Adjusted basis	$60,000	$18,637

Next, you figure the gain on each part, dividing your selling price and selling expenses between the two parts.

	Personal (3/4)	Business (1/4)
Selling price	$120,000	$40,000
Minus: Selling expenses	7,500	2,500
	$112,500	$37,500
Minus: Adjusted basis	60,000	18,637
Gain	52,500	18,863

Then, to figure your taxable gain and exclusion on each part, you decide to fill out a separate Worksheet 2 (Part 2) for each part, dividing your maximum exclusion between the two parts. You are single, so your maximum exclusion is $250,000.

Part 2 – Exclusion and Taxable Gain	Personal (3/4)	Business (1/4)
6) Depreciation after May 6, 1997	$–0–	$1,363
7) Subtract line 6 from gain	52,500	$17,500
8) Maximum exclusion	$187,500	$62,500
9) Exclusion (Smaller of line 7 or line 8)	52,500	17,500
10) Taxable gain (gain minus line 9)	–0–	$1,363
11) Smaller of line 6 or line 10	–0–	$1,363

You report the taxable gain from the business part ($1,363) on Form 4797. You do not report the gain from the other part on your return, because it is excluded in full.

Special Situations

The situations that follow may affect your exclusion.

Expatriates. You cannot claim the exclusion if section 877(a)(1) of the Internal Revenue Code applies to you. That section applies to U.S. citizens who have renounced their citizenship (and long-term residents who have ended their residency) if one of their principal purposes was to avoid U.S. taxes.

In addition, you cannot make the choice described on page 4. (You could make that choice if you sold your home before August 6, 1997.)

Home destroyed or condemned. If your home was destroyed or condemned, any gain (for example, because of insurance proceeds you received) qualifies for the exclusion.

Any part of the gain that cannot be excluded (because it is more than the limit) may be postponed under the rules explained in:

- Publication 547, in the case of a home that was destroyed, or
- Chapter 1 of Publication 544, in the case of a home that was condemned.

Sale of remainder interest. Subject to the other rules in this chapter, you can choose to exclude gain from the sale of a remainder interest in your home. If you make this choice, you cannot choose to exclude gain from your sale of any other interest in the home that you sell separately.

Exception for sales to related persons. You cannot exclude gain from the sale of a remainder interest in your home to a related person. Related persons include your brothers and sisters, half-brothers and half-sisters, spouse, ancestors (parents, grandparents, etc.), and lineal descendants (children, grandchildren, etc.). Related persons also include certain corporations, partnerships, trusts, and exempt organizations.

Reporting the Gain

Do not report the 1999 sale of your main home on your tax return unless:

- You have a gain and do not qualify to exclude all of it,
- You have a gain and choose not to exclude it, or
- You made the choice described on page 4 in this chapter and have a taxable gain.

If you have any taxable gain on the sale of your main home that cannot be excluded, report the entire gain realized (line 5 of Worksheet 2) on Schedule D (Form 1040), *Capital Gains and Losses.* Report it on line 1 or line 8 of Schedule D, depending on how long you owned the home. If you qualify for an exclusion (line 9 of Worksheet 2), show it on the line directly below the line on which you report the gain. Write "Section 121 exclusion" in column (a) of that line and show the amount of the exclusion in column (f) as a loss (in parentheses).

Choice made to use prior law rules. If you made the choice on page 4 and you sold your home in 1999, use Worksheet 4 on page 34 to figure your gain, one-time exclusion, taxable gain, and postponed gain. Report any taxable gain on Schedule D (Form 1040). You will not report an exclusion or a postponed gain on your return. You should keep the filled-in worksheet with your copy of your 1999 tax return.

Installment sale. Some sales are made under arrangements that provide for part or all of the selling price to be paid in a later year. These sales are called "installment sales." If you finance the buyer's purchase of your home yourself, instead of having the buyer get a loan or mortgage from a bank, you probably have an installment sale. If the sale qualifies, you can report the part of the gain you cannot exclude on the installment basis.

Use Form 6252 to report the sale. Enter your exclusion (line 9 of Worksheet 2) on line 15 of Form 6252.

Seller-financed mortgage. If you sell your home and hold a note, mortgage, or other financial agreement, the payments you receive generally consist of both interest and principal. You must report the interest you receive as part of each payment separately as interest income. If the buyer of your home uses the property as a main or second home, you must also report the name, address, and social security number (SSN) of the buyer on line 1 of either Schedule B (Form 1040) or Schedule 1 (Form 1040A). The buyer must give you his or her SSN and you must give the buyer your SSN. Failure to meet these requirements may result in a $50 penalty for each failure. If you or the buyer does not have and is not eligible to get an SSN, see the next discussion.

Individual taxpayer identification number (ITIN). If either you or the buyer of your home is a nonresident or resident alien who does not have and is not eligible to get an SSN, the IRS will issue you (or the buyer) an ITIN. To apply for an ITIN, file Form W–7, *Application for IRS Individual Taxpayer Identification Number*, with the IRS.

If you have to include the buyer's SSN on your return and the buyer does not have and cannot get an SSN, enter the buyer's ITIN. If you have to give an SSN to the buyer and you do not have and cannot get one, give the buyer your ITIN.

An ITIN is for tax use only. It does not entitle the holder to social security benefits or change the holder's employment or immigration status under U.S. law.

More information. For more information on installment sales, see Publication 537, *Installment Sales.*

Illustrated Example

Emily White, a single person, bought a home in 1988. She lived in the home until May 31, 1997, when she moved out of the house and put it up for rent. Emily rented her home until May 31, 1998. She moved back into the house and lived there until she sold it on January 10, 1999.

Emily can exclude gain on the sale of her home because she owned and lived in the home for at least 2 years of the 5-year period ending on the date of the sale.

Emily's records show the following:

1) Original cost	$50,000
2) Legal fees for title search	750
3) Back taxes paid for prior owner	1,500
4) Improvements (deck)	2,000
5) Selling price	195,000
6) Commission and expenses of sale	15,000
7) Depreciation claimed after May 6, 1997	1,642

Emily uses Worksheet 1 to figure the adjusted basis of the home she sold ($52,608). She uses Worksheet 2 to figure the gain on the sale ($127,392) and the amount of her exclusion ($125,750). Emily cannot exclude $1,642, the part of her gain equal to the depreciation deduction claimed while the house was rented. The completed worksheets and the front page of Emily's Schedule D appear on pages 17 and 18.

Chapter 2—1999 Sale of Main Home—Emily White

Worksheet 1. **Adjusted Basis of Home Sold**

Caution: *See if any of the situations listed in Table 1 apply to you before you use this worksheet.*

1.	Enter the purchase price of your old home. If you filed Form 2119 when you originally acquired your old home to postpone gain on the sale of a previous home, enter the adjusted basis of the new home from that Form 2119		**1.**	$50,000
2.	Seller-paid points, for home bought after 1990. (See *Seller-paid points* in this chapter.) Do not include any seller-paid points you previously subtracted to arrive at the amount entered on line 1, above		**2.**	
3.	Subtract line 2 from line 1		**3.**	50,000
4.	Settlement fees or closing costs. See *Settlement fees or closing costs* in this chapter. If line 1 includes the adjusted basis of the new home from Form 2119, go to line 6.			
a.	Abstract and recording fees	**a.**		
b.	Legal fees (including title search and preparing document)	**b.** 750		
c.	Surveys	**c.**		
d.	Title insurance	**d.**		
e.	Transfer or stamp taxes	**e.**		
f.	Amounts the seller owed that you agreed to pay (back taxes or interest, recording or mortgage fees, and sales commissions)	**f.** 1,500		
g.	Other	**g.**		
5.	Add lines 4a through 4g		**5.**	2,250
6.	Cost of capital improvements. Do not include any capital improvements included on line 1 above		**6.**	2,000
7.	Special tax assessments paid on your old home for local improvements, such as streets and sidewalks		**7.**	
8.	Other increases to basis		**8.**	
9.	Add lines 3, 5, 6, 7, and 8		**9.**	54,250
10.	Depreciation, related to the business use or rental of your old home, claimed (or allowable)	**10.** 1,642		
11.	Other decreases to basis (see *Decreases to basis* in this chapter.)	**11.**		
12.	Add lines 10 and 11		**12.**	1,642
13.	**ADJUSTED BASIS OF HOME SOLD.** Subtract line 12 from line 9. Enter here and on Worksheet 2, line 4		**13.**	$52,608

Worksheet 2. **Gain (or Loss), Exclusion, and Taxable Gain**

Part 1–Gain (or Loss) on Sale

1.	Selling price of home	**1.**	$195,000
2.	Selling expenses	**2.**	15,000
3.	Subtract line 2 from line 1	**3.**	180,000
4.	Adjusted basis of home sold. (From Worksheet 1, line 13.)	**4.**	52,608
5.	Subtract line 4 from line 3. This is the **gain** (**or loss**) on the sale. If this is a loss, stop here	**5.**	127,392

Part 2–Exclusion and Taxable Gain

6.	Enter any depreciation claimed on the property for periods after May 6, 1997. If none, enter zero	**6.**	1,642
7.	Subtract line 6 from line 5. (If the result is less than zero, enter zero.)	**7.**	125,750
8.	If you qualify to exclude gain on the sale, enter your maximum exclusion. (See *Maximum Amount of Exclusion* in this chapter.) If you do not qualify to exclude gain, enter -0-	**8.**	250,000
9.	Enter the smaller of line 7 or line 8. This is your exclusion	**9.**	125,750
10.	Subtract line 9 from line 5. This is your taxable gain. Report it as described under *Reporting the Gain* on page 15. If the amount on this line is zero, do not report the sale or exclusion on your tax return. **If the amount on line 6 is more than zero, complete line 11**	**10.**	1,642
11.	Enter the smaller of line 6 or line 10. Enter this amount on line 10 of the *Unrecaptured Section 1250 Gain Worksheet* in the instructions for Schedule D (Form 1040)	**11.**	$1,642

Schedule D for Emily White

SCHEDULE D (Form 1040)

Department of the Treasury
Internal Revenue Service

Capital Gains and Losses

▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040).

▶ Use Schedule D-1 for more space to list transactions for lines 1 and 8.

OMB No. 1545-0074

1999

Attachment Sequence No. 12

Name(s) shown on Form 1040: Emily White

Your social security number: 000 00 0000

Part I Short-Term Capital Gains and Losses—Assets Held One Year or Less

	(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5)	(e) Cost or other basis (see page D-5)	(f) GAIN or (LOSS) Subtract (e) from (d)
1						
2	Enter your short-term totals, if any, from Schedule D-1, line 2		2			
3	**Total short-term sales price amounts.** Add column (d) of lines 1 and 2		3			
4	Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824				4	
5	Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				5	
6	Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 1998 Capital Loss Carryover Worksheet				6	( )
7	**Net short-term capital gain or (loss).** Combine lines 1 through 6 in column (f) ▶				7	

Part II Long-Term Capital Gains and Losses—Assets Held More Than One Year

	(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price (see page D-5)	(e) Cost or other basis (see page D-5)	(f) GAIN or (LOSS) Subtract (e) from (d)	(g) 28% RATE GAIN or (LOSS) * (see instr. below)
8	main home	9/3/88	1/10/99	180,000	52,608	127,392	
	section 121 exclusion					(125,750)	
9	Enter your long-term totals, if any, from Schedule D-1, line 9		9				
10	**Total long-term sales price amounts.** Add column (d) of lines 8 and 9		10	180,000			
11	Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824				11		
12	Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				12		
13	Capital gain distributions. See page D-1				13		
14	Long-term capital loss carryover. Enter in both columns (f) and (g) the amount, if any, from line 13 of your 1998 Capital Loss Carryover Worksheet				14	( )	( )
15	Combine lines 8 through 14 in column (g)				15		
16	**Net long-term capital gain or (loss).** Combine lines 8 through 14 in column (f) ▶ **Next:** Go to Part III on the back.				16	1,642	

*28% Rate Gain or Loss** includes **all** "collectibles gains and losses" (as defined on page D-5) and up to 50% of the eligible gain on qualified small business stock (see page D-4).

For Paperwork Reduction Act Notice, see Form 1040 instructions. Cat. No. 11338H **Schedule D (Form 1040) 1999**

Real Estate and Transfer Taxes

When you sell your main home, treat real estate and transfer taxes on that home as discussed in this section.

Real estate taxes. You and the buyer must deduct the real estate taxes on your home for the year of sale according to the number of days in the real property tax year that each owned the home.

- ***You*** are treated as paying the taxes up to, but not including, the date of sale. You can deduct these taxes as an itemized deduction in the year of sale. It does not matter what part of the taxes you actually paid.
- ***The buyer*** is treated as paying the taxes beginning with the date of sale.

If the buyer paid your share of the taxes (or any delinquent taxes you owed), the payment increases the selling price of your home. The buyer adds the amount paid to his or her basis in the property.

If the person responsible for closing the sale (generally the settlement agent) must file Form 1099–S, the information reported on the form to you and the IRS must include (in box 5) the part of any real estate tax that the buyer can deduct. If you actually paid the taxes for the year of sale, you must subtract the amount shown in box 5 of Form 1099–S from the amount you paid. The result is the amount you can deduct.

For more information about real estate taxes, see Publication 530.

Transfer taxes. You cannot deduct transfer taxes, stamp taxes, and other incidental taxes and charges on the sale of a home as itemized deductions. However, if you pay these amounts as the seller of the property, they are expenses of the sale and reduce the amount you realize on the sale. If you pay these amounts as the buyer, include them in your cost basis of the property.

3. Rules Under Prior Law

The rules in this chapter are the rules that applied to sales of a main home before May 7, 1997. They have been kept in the publication because they may apply to you if you are in either of the following situations.

1) You sold your main home at a gain before May 7, 1997, and either:

   a) Bought a new home in 1999 within the replacement period, or

   b) Did not buy a new home before your replacement period ended in 1999.

2) You sold your main home at a gain in 1999, and made the choice described on page 4.

The main topics in this chapter are:

- Postponing gain,
- How and when to report, and
- One-time exclusion of gain.

Gain. If you had a gain from the sale, you must include it in your income for the year of sale, except for any part you postpone or exclude.

Loss. If you had a loss from the sale, you cannot deduct it.

How to report the sale. Generally, sales covered by this chapter were reported using **Form 2119**, *Sale of Your Home.*

You will ***not*** use Form 2119 if you sold your home in 1999 and make the choice to use the rules described in this chapter. (That choice is explained in chapter 2 on page 4.) In that case, use Worksheet 4 on page 34 to figure your gain, one-time exclusion, taxable gain, and postponed gain. If you have a taxable gain, report it on Schedule D (Form 1040). You will not report an exclusion or a postponed gain on your return. You should keep the filled-in worksheet with your copy of your 1999 tax return.

Postponing Gain

Under the rules of this chapter, you ***must*** postpone tax on the gain on the sale of your main home if both of the following are true.

1) You buy and live in a new main home within the replacement period.

2) The new main home costs at least as much as the adjusted sales price of the old home.

(Also, if you are age 55 or older and meet certain qualifications, no tax applies to any gain you choose to exclude. See *One-Time Exclusion of Gain,* later.)

This section of the chapter explains the time allowed for replacing your main home (the replacement period) and how to determine the taxable gain, if any. The main topics in this section are:

- Replacement period,
- Old home,
- New home, and
- Certain sales by married persons.

Tax postponed, not forgiven. The tax on the gain is postponed, not forgiven. You subtract any gain that is not taxed in the year you sell your old home from the cost of your new home. This gives you a lower basis in the new home.

Example. You sold your home in February 1997 for $90,000 and had a $5,000 gain. In January 1999, within the time allowed for replacement, you bought another home for $103,000 and moved into it. The $5,000 gain will not be taxed in 1997, but you must subtract it from the $103,000. This makes the basis of your new home $98,000. If you later sell the new home for $110,000, your gain will be $12,000 ($110,000 – $98,000).

Source of funds to buy home. You do not have to use the same funds received from the sale of your old home to buy or build your new home. For example, you can use less cash than you received by increasing the amount of your mortgage loan and still postpone the tax on your gain.

Replacement Period

Your replacement period is the time period during which you must replace your old home to postpone any of the gain from its sale. It starts ***2 years before*** and ends ***2 years after*** the date of sale.

Example. You sold your old home on April 27, 1997. You had until April 27, 1999, to buy and move into a new home that you use as your main home.

Occupancy test. You must physically live in the new home as your main home within the replacement period. If you move furniture or other personal belongings into the new home but do not actually live in it, you have not met the occupancy test.

No added time is allowed. To postpone gain on the sale of your home, you must replace the old home and occupy the new home within the specified period. You are not allowed any additional time, even if conditions beyond your control keep you from doing it (unless you qualify for a suspension of the replacement period, as explained later). For example, destruction of the new home while it was being built would not extend the replacement period. Also, if you bought or began building your new home within the specified period but for any reason were unable to live in it within 2 years, the replacement period is not extended.

If you do not replace the home in time and you had postponed gain in the year of sale, you must file an amended return for the year of sale. You must include in your income the entire gain on the sale of your old home. You will have to pay interest on any additional tax due. The interest is generally figured from the due date of the original return.

Suspension of replacement period. The replacement period may be suspended for:

- People living outside the United States, and
- Members of the Armed Forces.

The following chart illustrates the replacement period for most people and for those who qualify for the suspension. The chart uses the example of a home sold on April 30, 1997.

FOR ...	THE replacement period begins ...	AND the replacement period ends ...
Most people	2 years before the sale (April 30, 1995)	2 years after the sale (April 30, 1999).
Certain people living and working outside the United States	2 years before the sale (April 30, 1995)	4 years after the sale (April 30, 2001).
Members of the Armed Forces on extended active duty	2 years before the sale (April 30, 1995)	4 years after the sale (April 30, 2001).
Members of the Armed Forces stationed outside the United States	2 years before the sale (April 30, 1995)	8 years after the sale (April 30, 2005).
For details, including the special rules that apply to combat zone service, see the following discussions of *People Outside the United States* and *Members of the Armed Forces.*		

People Outside the United States

The replacement period after the sale of your old home is suspended while you have your ***tax home*** (the place where you live and work) outside the United States. This suspension applies only if your stay abroad begins before the end of the 2-year replacement period. The replacement period, plus the period of suspension, is limited to ***4 years*** after the date of sale of your old home.

Example. You sold your home on May 11, 1996. This began your replacement period. On September 11, 1996, you were transferred to a foreign country. You had used 4 months of your replacement period and had 20 months left. From September 11, 1996, to June 10, 1998, when you returned to the United States, your replacement period was suspended. Your replacement period started again on June 11, 1998, and ends 20 months later on February 11, 2000.

Married persons. If you are married, the suspension of the replacement period lasts while either you or your spouse has a tax home outside the United States, provided both of you used the old and the new homes as your main home.

Tax home. Your tax home is the city or general area of your main place of business, employment, station, or post of duty. For your tax home to be outside the United States, you must live and work there. It does not matter where your family lives. More information on a tax home outside the United States is in Publication 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad.*

Combat zone service. The running of the replacement period (including the suspension if you live and work outside the United States) is suspended for any period you served in a combat zone (defined later under *Members of the Armed Forces*) in support of the Armed Forces, plus 180 days. This suspension applies even though you were not a member of the Armed Forces. It applies to Red Cross personnel, accredited correspondents, and civilians under the direction of the Armed Forces in support of those forces.

The rules for suspending the running of the replacement period and for applying that suspension to your spouse are the same as the suspension rules explained later under *Members of the Armed Forces* and its discussion *Combat zone service.*

Members of the Armed Forces

The replacement period after the sale of your old home is suspended while you serve on extended active duty in the Armed Forces. You are on extended active duty if you are serving under a call or order for more than 90 days or for an indefinite period. The suspension applies only if your service begins before the end of the 2-year replacement period. The replacement period, plus any period of suspension, is limited to ***4 years*** after the date you sold your old home.

Example 1. You sold your home on May 1, 1996. This began your replacement period. You joined the Armed Forces on August 1, 1996. You had used 3 months of your replacement period (May, June, and July). Your active duty ended July 31, 1998. From August 1, 1996, to July 31, 1998, your replacement period was suspended. Your replacement period started again on August 1, 1998, and you have until May 1, 2000 (21 months) to buy or build and live in your new home.

Example 2. You are a regular member of the Armed Forces and sold your home on June 5, 1996. If you remain in the Armed Forces, you postpone your gain from the sale of your old home only if you buy or build and live in another home by June 5, 2000.

Overseas assignment. The suspension of the replacement period after the sale of your old home is extended for up to an additional 4 years while you are:

- Stationed outside the United States, or
- Required to live in on-base quarters following your return from a tour of duty outside the United States. In this case, you must be stationed at a remote site where the Secretary of Defense has determined that adequate off-base housing is not available.

The suspension can continue for up to 1 year after the last day you are stationed outside the United States or the last day you are required to live in government quarters on base. However, the replacement period, plus any period of suspension, is limited to ***8 years*** after the date of sale of your old home.

If you qualify for the time suspension for members of the Armed Forces and have already filed an income tax return reporting gain from the sale of a home that can be further postponed, you can file Form 1040X to claim a refund. See *Amended Return,* later, for the time allowed for filing an amended return.

Example 1. You are a regular member of the Armed Forces and sold your home on May 1, 1993. During the 4 years from May 1, 1993, to May 1, 1997, you served outside the United States. When you returned, you were stationed at a remote site and were required to live on base because off-base housing was not available. The time to replace your home was suspended:

1) While you were serving outside the United States, plus
2) While you were required to live on base after your return from the overseas assignment, plus
3) Up to 1 year.

The requirement that you live on base ended on October 31, 1997, so the suspension period expired October 31, 1998. You still have the full 2-year replacement period to buy or build and occupy a new home. This is because you did not use any of that time before your overseas assignment began, and your replacement period plus your 5½ year period of suspension is not more than 8 years. Your replacement period ends on October 31, 2000.

Example 2. The facts are the same as in Example 1 except the requirement that you live on base ended on October 31, 1998. The suspension period expired October 31, 1999. You have less than the full 2-year replacement period to buy or build and occupy a new home. This is because your replacement period plus your 6½-year period of suspension is limited to 8 years after the sale of your old home. Therefore, your replacement period ends on May 1, 2001.

Spouse in Armed Forces. If your spouse is in the Armed Forces and you are not, the suspension also applies to you if you owned the old home. Both of you must have used the old home and must use the new home as your main home. However, if you are divorced or separated while the replacement period is suspended, the suspension ends for you on the date of the divorce or separation.

Combat zone service. The running of the replacement period (including any suspension) is suspended for any period you served in a combat zone.

Combat zone. The term "combat zone" means:

1) The Persian Gulf Area combat zone (effective August 2, 1990),
2) The qualified hazardous duty area of Bosnia and Herzegovina, Croatia, and Macedonia, which is

treated as a combat zone effective November 21, 1995, and

3) The Federal Republic of Yugoslavia (Serbia/Montenegro), Albania, the Adriatic Sea, and the Ionian Sea north of the 39th parallel, effective March 24, 1999.

Service outside combat zone. If you performed military service in an area outside the combat zone that was in direct support of military operations in the combat zone ***and*** you received special pay for duty subject to hostile fire or imminent danger, you are treated as if you served in the combat zone.

Also, you are treated as if you served in a combat zone if you performed services as part of Operation Joint Endeavor, Operation Joint Guard, or Operation Allied Force, were outside the United States, and were deployed away from your permanent duty station.

When suspension ends. This suspension ends 180 days after the later of:

1) The last day you were in the combat zone (or, if earlier, the last day the area qualified as a combat zone), or

2) The last day of any continuous hospitalization (limited to 5 years if hospitalized in the United States) for an injury sustained while serving in the combat zone.

Example. Sergeant James Smith, on extended active duty in an Army unit stationed in Virginia, had a gain from the sale of his home on June 4, 1995. He had not yet purchased a new home when he entered a combat zone on January 4, 1996. He left the combat zone on January 4, 1997, and returned with his unit to Virginia. He remains on active duty in Virginia.

Sergeant Smith's replacement period began on June 4, 1995, the date he sold the home. If he had not been sent to a combat zone, his replacement period would have ended 4 years later, on June 4, 1999.

When he entered the combat zone on January 4, 1996, Sergeant Smith had used 7 months of the replacement period. The replacement period was then suspended for the time he served in the combat zone plus 180 days. The replacement period started again on July 4, 1997, after the end of the 180-day period (January 5, 1997, to July 3, 1997) following his last day in the combat zone. Sergeant Smith then has 41 months remaining in his replacement period (4 years minus the 7 months already used). His replacement period ends December 3, 2000 (41 months after July 3, 1997).

Spouse. The suspension for service in a combat zone generally applies to your spouse (even if you file separate returns). However, any suspension because of your hospitalization within the United States does not apply to your spouse. Also, the suspension for your spouse does not apply for any tax year beginning more than 2 years after the last day the area qualified as a combat zone.

More information. For information on other tax benefits available to those who served in a combat zone, get Publication 3, *Armed Forces' Tax Guide.*

Amended Return

If you sold your old home and did not plan to replace it, you had to include the gain in income for the year of sale. If you later change your mind, buy or build and live in another home within the replacement period, and meet the requirements to postpone gain, you will have to file an amended return (Form 1040X) for the year of sale to claim a refund.

You can file an amended return by the later of:

1) 3 years from the date you filed the return for the year of sale, or

2) 2 years from the date you paid the tax.

A return filed before the due date is treated as filed on the due date.

You may have longer to file the amended return if you could not manage your finances for a time due to a medically determinable physical or mental impairment that has lasted or can be expected to last for a continuous period of at least 12 months or can be expected to result in death. This does not apply if your spouse or someone else was authorized to act for you during that time. See Publication 556, *Examination of Returns, Appeal Rights, and Claims for Refund*, for more information.

Extended replacement period. If you have an extended replacement period because you have your tax home outside the United States or are a member of the Armed Forces, the replacement period may go beyond the last date you can file an amended return claiming a refund for the year of sale. If there is a possibility you may change your mind and buy (or build) and live in another home during the extended replacement period, you should file a “protective claim” for refund of the tax you paid on the gain. File this claim on Form 1040X anytime within the period allowed for filing an amended return.

Protective claim. To file a protective claim for refund, use Form 1040X and its instructions. However, you may leave lines 1 through 23 blank on the front of the form if you do not know the amount of your postponed gain. In *Part II* of the form:

1) Write “Protective Claim,”

2) Explain that you paid tax on the gain from the sale of your old home,

3) State the amount of the gain you reported on your original return,

4) State that you have an extended replacement period and why this extended period applies to your particular situation, and

5) State that you are filing this protective claim because during your extended replacement period you may buy (or build) a new main home.

Old Home

To figure the taxable gain and postponed gain from the sale of your old home, compare the ***adjusted sales price*** of your old home with the cost of your new home, as shown in the following chart.

IF the cost of your new home is ...	THEN you ...
Equal to or more than the adjusted sales price of your old home	Must postpone your entire gain. None of it is taxed in the year of sale.
Less than the adjusted sales price of your old home	Are taxed on the smaller of: ● The entire gain (minus any exclusion), or ● The difference between the adjusted sales price of the old home and the cost of the new home. You must postpone any gain that is not taxed.

Adjusted sales price. This is the amount realized from the sale of your old home minus:

- Any one-time exclusion you claim (line 14 of Form 2119), and
- Any fixing-up expenses you had (line 16 of Form 2119).

If the amount realized (minus any one-time exclusion) is not more than the cost of your new home, you postpone your entire gain. You do not need to figure your fixing-up expenses.

Fixing-up expenses. Fixing-up expenses are decorating and repair costs that you paid to sell your old home. For example, the costs of painting the home, planting flowers, and replacing broken windows are fixing-up expenses. Fixing-up expenses must meet all the following conditions. The expenses:

1) Must be for work done during the 90-day period ending on the day you sign the contract of sale with the buyer,
2) Must be paid no later than 30 days after the date of sale,
3) Cannot be deductible in arriving at your taxable income,
4) Must not be used in figuring the amount realized, and
5) Must not be capital expenditures or improvements.

Note. You subtract fixing-up expenses from the amount realized ***only*** in figuring the part of the gain that you postpone. You ***cannot*** use them in figuring the actual gain on the sale.

Example. Your old home had a basis of $55,000. You signed a contract to sell it on December 17, 1996. On January 7, 1997, you sold it for $71,400. Selling expenses were $5,000. During the 90-day period ending December 17, the date you signed the sales contract, you had the following work done. You paid for the work within 30 days after the date of sale.

Fixing-up expenses:
Inside and outside painting $800
Improvements:
New venetian blinds and new water heater $900

Within the replacement period, you bought and lived in a new home that cost $64,600. You figure the gain postponed and not postponed, and the basis of your new home, as follows:

Gain On Sale			
a)	Selling price of old home	$71,400	
b)	Minus: Selling expenses	5,000	
c)	Amount realized on sale		$66,400
d)	Basis of old home	$55,000	
e)	Plus: Improvements (blinds and heater)	900	
f)	Adjusted basis of old home		55,900
g)	Gain on sale [(c) minus (f)]		$10,500
Gain Taxed in Year of Sale			
h)	Amount realized on sale	$66,400	
i)	Minus: Fixing-up expenses (painting)	800	
j)	Adjusted sales price		$65,600
k)	Minus: Cost of new home		64,600
l)	Excess of adjusted sales price over cost of new home		$1,000
m)	Gain taxed in year of sale [lesser of (g) or (l)]		$1,000
Gain Postponed			
n)	Gain on sale [line (g)]	$10,500	
o)	Minus: Gain taxed [line (m)]	1,000	
p)	Gain postponed		$9,500
Adjusted Basis of New Home			
q)	Cost of new home [line (k)]	$64,600	
r)	Minus: Gain postponed [line (p)]	9,500	
s)	Adjusted basis of new home		$55,100

Property used partly as your home and partly for business or rental. You may use part of your property as your home and part of it for business or to produce income. If you sell the entire property, you should consider the transaction as the sale of two properties. You postpone the gain only on the part used as your home. This includes the land and outbuildings, such as a garage for the home, but not those used for the business or the production of income.

To postpone the gain on the part of the property that is your home (one property), you must reinvest an amount equal to that part's adjusted sales price in your new home. The same rule applies if you buy property for use as your home and for your business. Only the purchase price for the part used as your home can be counted as the cost of a new home. See *New home used partly for business or rental*, later.

For an example of how to divide the gain between the part of the property used as your home and the part used for business or other purposes, see *Business Use or Rental of Home* in chapter 2.

Home changed to rental property. You cannot postpone tax on the gain on rental property, even if you once used it as your home. The rules explained in this

chapter generally will not apply to its sale. Gains are taxable and losses are deductible as explained in Publication 544.

Temporary rental of home before sale. You have not changed your home to rental property if you temporarily rented out your old home before selling it, or your new home before living in it, as a matter of convenience or for another nonbusiness purpose. You postpone the tax on the gain from the sale if you meet the requirements explained earlier.

For information on how to treat the rental income you receive, see Publication 527.

Failed attempt to rent home. If you placed your home with a real estate agent for rent or sale and it was ***not*** rented, it is not considered business property or property held for the production of income. The postponement of gain rules explained in this chapter will apply to the sale.

Rental property last used as main home. Special rules apply to a gain from the sale of certain rental property. Under these rules, part or all of the gain is treated as ordinary income, up to the amount of "additional depreciation." This is called "depreciation recapture." The part of the gain that is ordinary income cannot qualify for capital gain treatment.

The depreciation recapture rules do ***not*** apply to property that you changed from rental property to your main home before selling it. Instead, you have one of two options.

1) If you postpone gain under the rules described in this chapter, you carry over the depreciation adjustments and the additional depreciation to the new home. If you later change your new home to rental property and then dispose of it, you may have to recapture depreciation on the old home as ordinary income.
2) If you do not postpone gain under the rules in this chapter, you treat all of the gain as capital gain.

For more information about depreciation recapture, see chapter 3 of Publication 544.

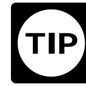
Rental property sold by persons age 55 or older. The depreciation recapture rules just described under *Rental property last used as main home* do not apply if:

- You were age 55 or older when you sold or otherwise disposed of rental property, and
- You owned and used that property as your main home at least 3 years out of the last 5 years. It does not matter whether, during your use of the property as your main home, you used all or part of it for rental purposes during vacations or seasonal absences.

This exception to the depreciation recapture rules applies even if you do not choose to exclude the gain from your gross income under the rules explained later under *One-Time Exclusion of Gain*. Instead, if you qualify, all the gain will be treated as capital gain, not ordinary income.

Condemned property. If your home was condemned for public use and you had a gain, you can postpone the tax on the gain in one of two ways. You can postpone the tax under:

- The rules explained earlier in this discussion of *Postponing Gain,* or
- The rules for a forced sale by condemnation explained next.



The replacement periods may differ for each treatment. You should compare them before deciding which rules to follow.

Rules for forced sale by condemnation. If you treat the transaction as a forced sale, you must buy replacement property that costs at least as much as the amount realized from the forced sale. The replacement period begins on the earlier of:

1) The date the condemned property was disposed of, or
2) The date condemnation was threatened.

The replacement period generally ends 2 years after the close of the first tax year in which you realize any part of the gain on the condemnation.

Example. You are a calendar year taxpayer. You were notified by the city council on March 6, 1995, of its plan to acquire your property, by condemnation if necessary. On May 3, 1997, when your property had an adjusted basis of $40,000, the city condemned the property and paid you $50,000. Your replacement period started on March 6, 1995, the date you were notified of the plan to condemn the property. Because you did not dispose of the property until 1997, your replacement period ends on December 31, 1999. This is 2 years after the last day of the year in which you realized the gain.

More information. Condemnations are discussed in detail in chapter 1 of Publication 544 under *Involuntary Conversions*.

Gain on casualty. The tax on a gain from a fire, storm, or other casualty cannot be postponed under the rules explained in this chapter, but may be postponed under rules similar to those discussed earlier in *Rules for forced sale by condemnation*. You can get additional information in Publication 547.

New Home

Your new home must be your main home. See the explanation of "main home" in chapter 1.

You must include in income any gain from the sale of your old home if you replace it with property that is not your main home.

New home outside the United States. A new home outside the United States qualifies as a new home for purposes of postponing gain. You must buy or build and live in the new home as your main home within the time allowed for replacement.

Retirement home. You have not purchased a new home if you invest in a retirement home project that gives you living quarters and personal care but does not give you any legal interest in the property. Therefore, you must include in income any gain on the sale of your old home. However, if you were age 55 or older on the date of the sale, see *One-Time Exclusion of Gain,* later.

Title to new home not held by you or spouse. You have not purchased a new home if you invest in a home in which neither you nor your spouse holds any legal interest (for example, a house to which someone else, such as your child, holds the title).

More than one new home bought in 2-year period. If you buy (or build) and live in more than one main home during the 2-year replacement period, only the last one can be treated as your new main home to determine whether you must postpone the gain from the sale of the old home.

Work-related move. The rule just described does not apply if you had to sell one new home and buy another one because of a work-related move. A work-related move is one for which you are allowed a deduction for moving expenses. To qualify for the deduction, the move must be closely related to the start of work, and you must meet the time and distance requirements explained in Publication 521.

Example. You buy two new homes and sell one of them as shown below:

April 1997	You sell your house in **Chicago** at a gain.
June 1997	You buy and move into a more expensive house in **Memphis**.
January 1999	You sell your house in **Memphis** due to a transfer required by your employer.
February 1999	You buy and move into a more expensive house in **New York City**. The move meets the requirements for a moving expense deduction.

When you completed the Form 2119 for the sale of your house in Chicago, you compared its adjusted sales price with the cost of the home bought in Memphis. This determined the gain you postponed. You do not need to refigure your postponed gain when you buy the home in New York City because your move to New York was work related.

For the tax treatment of the 1999 sale of the Memphis house, see chapter 2.

Holding period. If you postponed tax on any part of the gain from the sale of your old home, you will be considered to have owned your new home for the combined period you owned both the old and the new homes. This may affect how any taxable gain when you sell the new home is reported on Schedule D (Form 1040).

How To Figure Cost of New Home

You need to know the cost of your new home to figure the gain taxed and the gain on which tax is postponed on the sale of your old home. The cost of your new home includes costs incurred within the replacement period (beginning 2 years before and ending 2 years after the date of sale) for the following items:

1) Buying or building the home,

2) Rebuilding the home, and

3) Capital improvements or additions.

You cannot consider any costs incurred before or after the replacement period. However, if you live outside the United States or you are a member of the Armed Forces, you can include any costs incurred during the suspension period (discussed under *Replacement Period,* earlier).

Debts on new home. The cost of a new home includes the debts it is subject to when you buy it (purchase-money mortgage or deed of trust) and the face amount of notes or other liabilities you give for it.

Temporary housing. If a builder gives you temporary housing while your new home is being finished, you must reduce the contract price to arrive at the cost of the new home. To figure the amount of the reduction, multiply the contract price by a fraction. The numerator is the value of the temporary housing, and the denominator is the sum of the value of the temporary housing plus the value of the new home.

Seller-paid points. In figuring the cost of your new home, you must subtract any points paid by the seller from your purchase price.

Settlement fees or closing costs. The cost of your new home includes the settlement fees and closing costs that you can include in your basis. See *Settlement fees or closing costs* under *Basis,* in chapter 2.

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

Deductible costs. If you itemize your deductions in the year you buy the house, you can deduct some of the costs you paid at closing, such as real estate taxes, mortgage interest, and “points” that are deductible as interest. You may also be able to deduct points paid by the seller at closing. For more information, see Publication 936 and Publication 530.

Real estate taxes. If you agree to pay taxes the seller owed on your new home (that is, taxes up to the date of sale), the taxes you pay are treated as part of the cost. You cannot deduct them as taxes paid. If the seller paid taxes for you (that is, taxes beginning with the date of sale), you can still deduct the taxes. If you do not reimburse the seller for your part of the taxes, you must reduce the purchase price of your new home by the amount of those taxes. For more information, see *Settlement or closing costs* under *Basis* in Publication 530.

New home used partly for business or rental. If you replace your old home with property used partly as your home and partly for business or rental, you consider only the cost of the part used as your home. You must compare the cost of this part to the adjusted sales price

of the old home to determine the amount of gain taxed in the year of sale and the amount of gain on which tax is postponed.

Example. Your old home had a basis of $50,000. You sold it in February 1997 for a gain of $25,000. Your adjusted sales price is $75,000. In March 1998, you bought a duplex house for $120,000. You live in half and rent the other half. Because only half of the cost of the duplex ($60,000) is considered an investment in a new main home, you are taxed on $15,000 ($75,000 adjusted sales price – $60,000 cost) of the $25,000 gain on the sale. You must postpone tax on $10,000 of the gain reinvested in your new home. The basis of your new home is $50,000 ($60,000 cost – $10,000 postponed gain). The basis of the rented part of the duplex is $60,000.

Inheritance or gift. If you receive any part of your new home as a gift or an inheritance, you cannot include the value of that part in the cost of the new home when figuring the gain taxed in the year of sale and the gain on which tax is postponed. However, you include the basis of that part in your adjusted basis to determine any gain when you sell the new home.

Example. You bought a home in 1992 for $60,000. You sold that home in March 1997 for $65,000, at a gain of $5,000. You had fixing-up expenses of $200.

Your father died in November 1998 and you inherited his home. Its basis to you is $62,000. You spent $14,000 to modernize the home, resulting in an adjusted basis to you of $76,000. You moved into the home in February 1999.

To find the gain taxed in the year of the sale, you compare the adjusted sales price of the old home, $64,800 ($65,000 – $200), with the $14,000 you invested in your new home. (For this purpose, you do not include the value of the inherited part of your property, $62,000, in the cost of your new home.) The $5,000 gain is fully taxed because the adjusted sales price of the old home is more than the amount you paid to remodel your new home, and the difference between the two amounts is more than $5,000.

Certain Sales by Married Persons

This section explains how married persons figure their postponed gain in certain situations.

Home owned separately by one spouse. You may be able to postpone gain from the sale of your old home even if:

- You or your spouse owned the old home separately, but title to the new one is in both your names as joint tenants, or
- You and your spouse owned the old home as joint tenants, and either you or your spouse owns the new home separately.

You and your spouse can figure the postponed gain, which reduces the basis of the new home, as if the two of you owned both homes jointly. To do this, both of you must meet both of the following requirements.

- You used the old home as your main home and you use the new home as your main home.
- You sign a statement that says: “We agree to reduce the basis of the new home by the gain from selling the old home.”

Both of you must sign the statement. You can make the statement in the bottom margin on page 1 of Form 2119 or on an attached sheet. If either of you does not sign the statement, you must report the gain in the regular way, as explained in the following examples.

Example 1. In April 1997 you sell a home that you owned separately but that both you and your spouse used as your main home. The adjusted sales price is $98,000, the adjusted basis is $86,000, and the gain on the sale is $12,000. In February 1999 you and your spouse buy a new home for $100,000. You move in immediately. The title is held jointly, and under state law, you each have a one-half interest. If you both sign the statement to reduce the basis of the new home, you postpone the gain on the sale as if you had owned both the old and new homes jointly. You and your spouse will each have an adjusted basis of $44,000 ($50,000 cost minus $6,000 postponed gain) in the new home.

If either of you does not sign the statement, your entire gain of $12,000 will be currently taxed, not postponed. This is because the adjusted sales price of the old home ($98,000) is greater than your part of the cost of the new home ($50,000). You and your spouse will each have a basis of $50,000 in the new home.

Example 2. The facts are the same as in Example 1 except that you and your spouse owned the old home jointly and each had a one-half interest under state law. Your spouse buys the new home with separate funds and takes title individually. If you both sign the statement, you and your spouse postpone the $12,000 gain from the sale of the old home. Your spouse will have an adjusted basis of $88,000 ($100,000 cost – $12,000 postponed gain) in the new home.

If either of you does not sign the statement, you will be taxed on your share of the gain on the old home, but your spouse will postpone tax on his or her share of the gain. This is because the cost of the new home was more than your spouse's share of the adjusted sales price of the old home. Your spouse's basis in the new home will be $94,000 ($100,000 cost – $6,000 postponed gain).

Example 3. The facts are the same as in Example 1 except that you own the old home individually and your spouse owns the new home individually. If you both sign the statement, you postpone the $12,000 gain from the sale of the old home. Your spouse will have an adjusted basis in the new home of $88,000.

If either of you does not sign the statement, your entire gain will be taxed, and your spouse's basis in the new home will be $100,000.

Deceased spouse. If your spouse dies after you sell your old home and before you buy and occupy a new home, you can postpone the gain from the sale of the old home if the basic requirements are met, and:

1) You were married on the date your spouse died, and

2) You use the new home as your main home.

This applies whether title to the old home is in one spouse's name or held jointly.

If you sold your home and did not postpone the entire gain on the sale because of the death of your spouse (but otherwise qualified to do so under the rules explained in this chapter), you can file an amended return (Form 1040X) to postpone the entire gain. See *Time to exclude gain,* later, under *One-Time Exclusion of Gain* and its discussion *How To Make and Revoke a Choice To Exclude Gain* for information about the time allowed to file an amended return.

Separate homes replaced by single home. If you and your spouse both had gains from the sales of homes that had been your separate main homes before your marriage, you may have to postpone the tax on both gains. This can happen if all of the following are true.

- You jointly purchase a new home.
- Each spouse's share of the cost of the new home is at least as much as the adjusted selling price of that spouse's old home. (Each spouse's share of the cost of the new home is the part equal to his or her interest in the home under state law, generally one-half.)
- Each spouse occupies the new home within the replacement period.

Example. Before your marriage in February 1997, you sold your old home for an adjusted sales price of $90,000, and your spouse sold her old home for an adjusted sales price of $110,000. You each realized a gain of $15,000 from your sale. After your marriage, you jointly purchased a new home at a cost of $200,000 and moved into it within the replacement period. Under state law, you each have a one-half interest in the new home.

You must postpone your gain since you are treated as purchasing a new home for $100,000 (½ of $200,000).

For the year of sale, there is tax on $10,000 of your spouse's gain. This is the amount by which the adjusted sales price of her old home is more than her $100,000 share of the cost of the new home.

Report the sales of the old homes on separate Forms 2119.

Home replaced by two homes of spouses living apart. If you and your spouse each buy and live in separate new homes, the postponement provisions apply separately to your gain and to your spouse's gain.

Example. You and your spouse owned your home jointly and used it as your main home. In April 1997, you sold the home for $98,000. The gain on the sale was $20,000. Under state law, each of you is entitled to one-half of the proceeds of the sale. Therefore, each of you had a $10,000 gain from the sale of your home.

In January 1999, you and your spouse also individually bought and lived in separate homes. The cost of each new home, $71,000 and $75,000 respectively, was more than your respective shares of the adjusted sales price of the old home. You and your spouse must postpone the tax on the $20,000 gain on the old home.

Your new home has an adjusted basis of $61,000 ($71,000 – ½ of $20,000 gain postponed). Your spouse's new home has an adjusted basis of $65,000 ($75,000 – ½ of $20,000 gain postponed).

You report the sale of your home on two Forms 2119 as if two separate properties were sold. You each report half of the sales price.

Only one spouse buys a new home. Even if your spouse does not buy a new home within the replacement period, you still should report on your Form 2119 only your share of any gain from the sale of the old home. You postpone your share of the gain if you meet all the requirements to do so, even though your spouse cannot postpone his or her share.

If you and your spouse originally filed a joint return for the year of sale, you and your spouse must file an amended joint return to report your spouse's share of the gain, which cannot be postponed. See *Divorce after sale* under *How and When To Report,* later.

How and When To Report

If you sold your main home in 1998 or 1999 and the rules in this chapter apply to you because you made the choice described on page 4, report the sale as explained under *Choice made to use prior law rules* on page 16.

Sales Before 1998

If you sold your main home before 1998 and the rules in this chapter apply to you (either because you sold the home before May 7, 1997, or because you made the choice described on page 4), the reporting requirements you may have are explained in this section.

Form 2119. For sales before 1998, Form 2119 was used to report the sale of an old home and any purchase of a new one within the replacement period. You should have filed Form 2119 with your tax return for the year you sold your old home. If you filed your return for that year before buying a new home, you may also have to file a second Form 2119 when you do buy your new home. If you need Form 2119 for that purpose, you can still order it from the IRS. See chapter 5. A filled in Form 2119 is shown at the end of this chapter.

Keep a copy of Form 2119 with your tax records for the year of the sale. Form 2119 is also a supporting document that shows how your new home's basis is decreased by the amount of any postponed gain on the sale of your old home. Therefore, you should also keep a copy of Form 2119 with your records for the basis of your new home.

Loss reported on sale. If you reported a loss on the sale of your home, you do not have to file a second Form 2119 if you later buy a new home. The loss on

the sale was not deductible and has no effect on the basis of your new home.

Reporting one-time exclusion. If you must file a second Form 2119 and qualify for the one-time exclusion of gain, use Form 2119 to claim the exclusion. See *One-Time Exclusion of Gain,* later, for details.

Reporting a taxable gain. Any taxable gain on the sale is reported on Schedule D (Form 1040).

New home purchased after return filed. If you postponed gain from the sale of your old home and you buy and live in a new home after you file your return for the year of the sale but within the replacement period, you should notify the IRS by filing a second Form 2119 and, if necessary, Form 1040X and Schedule D.

Send the form (or forms) to the Internal Revenue Service Center where you will file your next tax return.

New home costs at least as much as adjusted sales price. If your new home costs at least as much as the adjusted sales price of your old home, file the second Form 2119 by itself. This form must include your address, signature, and the date. If you filed a joint return for the year of sale, the form must also include your spouse's signature.

New home costs less. If your new home costs less than the adjusted sales price of the old home, you must file an amended return (Form 1040X) for the year of sale. Attach a second completed Form 2119 to report the purchase and Schedule D (Form 1040) showing the gain you must report. You will have to pay interest on any additional tax due. The interest is generally figured from the due date of the original return.

New home purchased after tax paid on gain. If you paid tax on the gain from the sale of your old home, and you buy and live in a new home within the replacement period, you must file an amended return (Form 1040X) for the year of sale of your old home. Complete a new Form 2119 and include it with your amended return. Report on Schedule D (Form 1040) any gain on which you cannot postpone the tax, and claim a refund of the rest of the tax.

Improvements made after tax paid on gain. If you replaced your old home but still had to pay tax on at least part of the gain from its sale, and you make improvements to your new home within the replacement period, fill out a new Form 2119 to refigure your taxable gain. If your refigured taxable gain is less than the gain you originally reported, file an amended return and include the new Form 2119.

No new home within replacement period. If you postponed gain on the sale of your old home because you planned to replace it but you do not replace it within the replacement period, you will have to file a second Form 2119. Attach it to an amended return (Form 1040X) for the year of the sale. Include a Schedule D (Form 1040) to report your gain.

You will have to pay interest on the additional tax due. Interest is generally figured from the due date of the original return.

Divorce after sale. If you are divorced after filing a joint return on which you postponed the gain on the sale of your home, but you do not buy or build a new home (and your former spouse does), you must file an amended joint return to report the tax on your share of the gain. If your former spouse refuses to sign the amended joint return, attach a letter explaining why your former spouse's signature is missing.

Installment sale. If you finance the buyer's purchase of your home yourself, instead of having the buyer get a loan or mortgage from a bank, you may have an installment sale. If the sale qualifies, you can report any part of the gain you cannot postpone or exclude on the installment basis. For information on reporting income from this type of sale, see *Installment sale* under *Reporting the Gain* in chapter 2.

Statute of limitations. The 3-year limit for assessing tax on the gain from the sale of your home begins when you give the IRS information that shows that:

1) You replaced your old home, and how much the new home cost,
2) You do not plan to buy and occupy a new home within the replacement period, ***or***
3) You did not buy and occupy a new home within the replacement period.

This information may be on the Form 2119 attached to your tax return for the year of the sale, or on a second Form 2119 filed later. File the second Form 2119 with the Service Center where you will file your next tax return. If needed, send an amended return for the year of the sale to include in income the gain that you cannot postpone.

Example

Frank and Evelyn Smith sold their home on May 1, 1997, for $87,000. They spent $500 on fixing-up expenses and paid a commission on the sale of $5,200. Neither Frank nor Evelyn was 55 or older on the date of the sale. They planned to buy a replacement home, but had not bought one before they filed their 1997 tax return.

Frank and Evelyn completed Part 1 of Form 2119 and attached it to their 1997 return. Because they planned to buy a replacement home, they did not include the gain on the sale in the income reported on their return.

On April 20, 1999, within the replacement period, Frank and Evelyn bought and moved into a new home. The cost of the new home was $77,200. This was less than the adjusted sales price of the old home. They figure the gain, the part of the gain on which tax is postponed and the part on which it is not, and the adjusted basis of their new home in the following way:

Gain On Sale

a) Selling price of old home	$87,000	
b) Minus: Selling expenses	5,200	
c) Amount realized on sale		$81,800
d) Minus: Adjusted basis of old home		63,000
e) Gain on sale		$18,800

Gain Taxed in 1997		
f) Amount realized on sale	$81,800	
g) Minus: Fixing-up expenses	500	
h) Adjusted sales price		$81,300
i) Minus: Cost of new home		77,200
j) Excess of adjusted sales price over cost of new home		$4,100
k) Gain taxed in 1997 [lesser of (e) or (j)]		$4,100

Gain Not Taxed in 1997		
l) Gain on sale [line (e)]	$18,800	
m) Minus: Gain taxed in 1997 [line (k)]	4,100	
n) Gain not taxed in 1997		$14,700

Adjusted Basis of New Home		
o) Cost of new home [line (i)]	$77,200	
p) Minus: Gain not taxed in 1997 [line (n)]	14,700	
q) Adjusted basis of new home		$62,500

The Smiths file Form 1040X to amend their 1997 return to include in income the part of their gain on which tax is not postponed. They attach a second Form 2119 and a Schedule D (Form 1040) that includes the taxable part of the gain. The filled-in Form 2119 they filed with their amended return appears at the end of this chapter.

One-Time Exclusion of Gain

This section discusses the exclusion from gross income of all or part of your gain from the sale of your main home if you met certain age, ownership, and use tests at the time of the sale. This was a one-time exclusion of gain for sales after July 26, 1978, and before May 7, 1997. However, for sales after May 6, 1997, you may qualify for the exclusion described in chapter 2.

(For certain sales after May 6, 1997, you may choose instead to claim the one-time exclusion and use the other rules described in this chapter. See page 4 for details on this choice.)

If you met the requirements discussed in this section and you make the choice to exclude gain on the sale of your main home, the excluded gain is not taxed.

If you change your mind after you file the return for the year of sale, you may be able to make or revoke the choice later. You would have to file an amended return for the year of sale within certain time limits. See *How To Make and Revoke a Choice To Exclude Gain,* later.

Exclusion Amount

If you met the age, ownership, and use tests, you can choose to exclude $125,000 of your gain on the sale of your home. If you were married on the date of the sale and file a separate return, you can only choose to exclude $62,500. Your gain is the amount realized on the sale minus the adjusted basis of the home. If there is gain remaining after the exclusion, you may have to postpone tax on the rest of the gain if, as explained earlier, you buy and live in another home.

Age, Ownership, and Use Tests for Sales Before May 7, 1997

You can claim the exclusion if you met ***all*** the following tests.

1) You were age ***55 or older*** on the date of the sale.
2) During the ***5-year period*** ending on the date of the sale, you:
   a) ***Owned*** your main home for at least ***3 years,*** and
   b) ***Lived in*** your main home for at least ***3 years***.
3) Neither you nor your spouse have ever excluded gain on the sale of a home after July 26, 1978. However, see *Effect of Marital Status,* later, for more details.

Age 55 at time of sale. You must have been 55 by the date you sold the home to qualify for the exclusion. You do not meet the age 55 test if you sell the property during the year in which you will be 55 but before you actually become 55. The earliest date on which you can sell your home and still qualify for the exclusion is your 55th birthday.

Ownership and use tests. The required 3 years of ownership and use (during the 5-year period ending on the date of the sale) do not have to be continuous. You meet the tests if you can show that you owned and lived in the property as your main home for either 36 full months or 1,095 days (365×3) during the 5-year period. Short temporary absences for vacations or other seasonal absences, even if you rent out the property during the absences, are counted as periods of use. See *Ownership and use tests met at different times,* later.

Example 1. From 1990 through 1994 Joseph Mooney lived with his son and daughter-in-law in a house owned by his son. On January 5, 1995, he bought this house from his son. He continued to live there until January 29, 1997, when he sold it. Although Joseph ***lived in*** the property as his main home for more than 3 years, he cannot exclude his gain on the sale. This is because he did not ***own*** the property for the required 3 years.

Example 2. Professor John Thomas bought and moved into a house on January 4, 1994. He lived in it as his main home continuously until February 1, 1996, when he went abroad for a 1-year sabbatical leave. During part of the period of leave, the property was unoccupied, and during the rest of the period, he rented it out. On March 4, 1997, he sold the house. Because his leave was not a short temporary absence, he cannot include the period of leave to meet the test of living in the house as his main home for 3 years or more. He cannot exclude his gain from income because he did not live in the house for the required period.

Ownership and use tests met at different times. You can meet the ownership and use tests during different 3-year periods. However, you must meet both tests during the 5-year period ending on the date of the sale.

Example. In 1990, Grace Jones was 50 years old and lived in a rented apartment. The apartment building was later changed to a condominium and she bought her apartment on December 1, 1993. In 1995, Grace became ill and on April 14 of that year she moved to

her daughter's home. On February 14, 1997, while still living in her daughter's home, she sold her apartment.

Grace can exclude gain on the sale of her apartment because she met the age, ownership, and use tests. Grace was over 55 at the time of the sale. Her 5-year period is from February 15, 1992, to February 14, 1997, the date she sold the apartment. She owned her apartment from December 1, 1993, to February 14, 1997 (over 3 years). Grace lived in the apartment from February 15, 1992, to April 14, 1995 (over 3 years).

Joint owners who are married. Both you and your spouse will meet the age, ownership, and use tests if you meet ***all*** of the following requirements.

1) You hold the home either as joint tenants, tenants by the entirety, or community property on the date of the sale.
2) You file a joint return for the tax year in which you sell the home.
3) ***Either*** you or your spouse has met the age, ownership, and use tests.

Joint owners who are not married. If the joint owners of a home were not husband and wife, each owner who chooses to exclude gain from income must meet the age, ownership, and use tests. If one owner meets the tests, that does not automatically qualify the other owners to exclude their gain from income.

Each owner excludes gain on an individual basis. If one owner chooses to exclude gain, the other owners do not have to exclude their gain.

Example. Frank Williams and his sister, Mary, each own a one-half interest in their jointly owned home. Frank meets the age, ownership, and use tests, but Mary does not. The adjusted basis of the home is $28,000, or $14,000 each. They sell the home in February 1997 for $180,000. Frank's interest in the amount realized is $90,000 (½ × $180,000). He can choose to exclude from gross income his entire gain of $76,000 ($90,000 − $14,000). Mary's gain is also $76,000, but she cannot exclude it. Mary must postpone tax on her gain if she meets the requirements explained earlier under *Postponing Gain.* If not, she must include her gain in income for the year of sale.

Previous home destroyed or condemned. For the ownership and use tests, you add the time you owned and lived in a previous home that was destroyed or condemned to the time you owned and lived in the home on which you wish to exclude gain. This rule applies if any part of the basis of the home you sold depended on the basis of the destroyed or condemned home. Otherwise, you must have owned and lived in the ***same*** home for 3 of the 5 years before the sale to qualify for the exclusion.

Exception for individuals with a disability. There is an exception to the 3-out-of-5-year use test if you become physically or mentally unable to care for yourself at any time during the 5-year period.

You qualify for this exception to the use test if, during the 5-year period before the sale of your home:

1) You became physically or mentally unable to care for yourself, and
2) You owned and lived in your home as your main home for a total of at least 1 year.

Under this exception, you are considered to live in your home during any time that you own the home and reside in a facility (including a nursing home) that is licensed by a state or political subdivision to care for persons in your condition.

If you meet this exception to the use test, you still have to meet the 3-out-of-5-year ownership test to claim the exclusion.

Home of spouse who died. You will meet the ownership and use tests if your spouse is deceased on the date you sell your main home, and:

1) You have not remarried,
2) Your deceased spouse had met the ownership and use tests for that main home, and
3) Your deceased spouse had not previously chosen or joined in choosing to exclude gain on the sale of another main home after July 26, 1978.

You must still meet the age test (be at least age 55 on the date of sale) to qualify for the exclusion.

Example. Ellen and Doug were married January 6, 1995. After their marriage, their main home was property Doug had owned and lived in as his main home since 1985. Doug died on January 2, 1997. He had never chosen or joined in choosing to exclude gain on the sale of any home.

Ellen inherited the property and continued to live in it as her main home until April 10, 1997, when she sold it. At the date of sale she was 56 years old, had not remarried, and had never chosen or joined in choosing to exclude gain on the sale of any home. Ellen can choose to exclude up to $125,000 of the gain from the sale of her home. This is because she meets the age test and Doug met the 3-out-of-5-year ownership and use tests for the property.

Sale by executor. Gain from the sale of a home by the executor of an estate may qualify for this exclusion. To qualify, the sale must be made under a contract entered into before death by a taxpayer who met the age, ownership, and use tests.

Rent-controlled apartment. If you receive a payment to give up your rights in a rent-controlled apartment, this gain does not qualify for the exclusion. You do not meet the ownership test when you rent an apartment.

Part of property used as main home. You may use only part of the property as your main home, as explained in chapter 2 under *Property used partly as your home and partly for business or rental.* In this case, you can claim an exclusion only for the gain on the part of the property used as your main home.

Example. Dr. Martin Russell met the age, ownership, and use tests when he sold his main home. However, for the whole time he owned the home, he used half of it exclusively as an office for treating his patients. Only the half of the property used as his home qualifies for the exclusion.

For an example of how to divide the gain between the part of the property used as your home and the part used for business or other purposes, see *Property used partly as your home and partly for business or rental* in chapter 2.

Note. If the business use of your old home was not more than 2 years of the 5-year period ending on the date of the sale, you do not have to divide the gain. However, you must decrease your basis in the old home by the depreciation allowed or allowable for the business use of it.

Gain From Casualty or Condemnation

You can exclude gain if your home was destroyed by a casualty or condemned.

Home destroyed. If your home was destroyed by fire, storm, or other casualty, you can choose to exclude gain from insurance proceeds or other compensation. You must follow the rules explained earlier in this section. However, if you have any gain remaining after the exclusion, you cannot postpone the tax on the rest of the gain by using the rules explained earlier under *Postponing Gain.* The rest may qualify, however, under the postponement-of-gain rules explained in Publication 547.

Home condemned. If your home was condemned for public use, you can treat the transaction as a sale of the home. If you choose to exclude gain from the condemnation, you must follow the rules explained earlier in this section. If you have any gain remaining after the exclusion, you may have to postpone the tax on the rest of the gain as explained earlier under *Postponing Gain.* Or, you can postpone it under the rules for a condemnation, as explained under *Involuntary Conversions* in chapter 1 of Publication 544.

Effect of Marital Status

For purposes of the exclusion, your marital status is determined as of the date of sale of your home. If you are legally separated under a decree of divorce or of separate maintenance, you are not considered married.

Your marital status on the date of the sale determines:

- The amount you can exclude,
- Whether your spouse must join you in the choice to exclude gain, and
- Whether each spouse can choose to exclude gain later.

Married persons must choose exclusion jointly. If you are married when you sell your main home, you cannot choose to exclude the gain unless your spouse joins you in making the choice. Your spouse must join you in the choice even if:

1) You or your spouse owned the home separately,
2) You and your spouse file separate returns, or
3) The spouse not owning an interest in the home had not lived in it for the required period before the sale.

Death of spouse after sale. If your spouse died after the sale, but before making the choice to exclude the gain, his or her personal representative (administrator or executor, for example) must join with you in making the choice. You, as the surviving spouse, are considered the personal representative of your deceased spouse if no one else has been appointed.

Home not jointly owned. If the home was not jointly owned, the spouse who owns it must meet the age, ownership, and use tests. The other spouse must join in making the choice.

Separate return. If you are married on the date of sale, file a separate return, and meet the age, ownership, and use tests, you can exclude no more than $62,500 of gain on the sale of your main home. Your spouse must show agreement to your choice by writing in the bottom margin on page 1 of Form 2119, or on an attached statement, “I agree to the Part II election.” Your spouse must also sign his or her name.

You or your spouse can exclude gain only once. If you or your spouse chooses to exclude gain from a sale after July 26, 1978, neither of you can choose to exclude gain again under the rules described in this chapter. (You may be able to exclude gain on a sale after May 6, 1997, under the rules in chapter 2.) The following chart shows how this rule applies in certain specific situations.

IF ...	THEN ...
You and your spouse owned separate homes before your marriage and sold both homes after your marriage	You can exclude the gain on one of them, but not on both.
You or your spouse excluded gain from a home sold before the marriage (and after July 26, 1978)	The spouse who excluded gain cannot join in another choice to exclude gain. If the couple sells a home during their marriage, neither can exclude any gain.
You or your spouse chooses to exclude gain from a sale made after July 26, 1978, and you later divorce	Neither of you can choose to exclude gain again. If you remarry, you and your new spouse cannot exclude gain on sales after your marriage. (But you may be able to revoke the earlier choice, as explained later.)

Sale before marriage. If you meet the age, ownership, and use tests when you sell your separately owned home during the year, you can exclude gain up to $125,000. If you marry before the end of the year, you can take the exclusion whether you file a joint return or a separate return. This is because you were single on the date of the sale.

Joint exclusion not required. If one spouse sells a home before the marriage, the other spouse does not have to join in the choice to exclude gain. The spouse who did not join in that choice is eligible to exclude gain if he or she later sells a house, meets the age, ownership, and use tests, and at the time of sale is single or married to a different spouse who has never excluded gain or joined in a choice to do so.

You can exclude gain only once. If one spouse excludes gain from a house sold before marriage, that spouse cannot join in another choice to exclude gain. If this couple then sells a home during their marriage, neither can exclude any gain under the rules in this chapter. This is because both spouses have to join in the choice, and one spouse has already excluded gain. However, see chapter 2 for sales after May 6, 1997.

Example 1 — sale before marriage. Joe Johnson and Betty Smith were single and each owned a home. In January 1997, they sold their homes and each had a gain of $125,000, for a total gain of $250,000. Each met the age, ownership, and use tests at the time of sale.

Later that year, Joe and Betty married. Because Joe and Betty were single when they sold their homes, they each can choose to exclude $125,000 of gain ($250,000 total). This is true whether they file a joint return or separate returns.

Example 2 — sales before marriage and after marriage ends. Tom Oak sold his main home in 1996. He met the age, ownership, and use tests to exclude gain on the sale. Later in the year of sale, he married Susan Green. They filed a joint return for that year and Tom chose to exclude the gain on the sale of his house. Susan did not have to join in Tom's choice since they were not married on the date of the sale.

While married, Tom and Susan lived in Susan's separately owned house. Tom died in January 1997, and Susan sold her house in February 1997. She met the age, ownership, and use tests to exclude gain on the sale. She can exclude up to $125,000 of the gain. This is because she was single on the date of sale and she has never made a choice to exclude gain before. She did not have to join in Tom's choice.

Example 3 — separate returns. David and Beth Pine sold their jointly owned home in March 1997. They both met the ownership and use tests at the time of sale, but David was 62 and Beth was 50. They decide to file separate returns for 1997. Because Beth did not meet the age test, she cannot choose to exclude gain on her separate return. David can choose to exclude up to $62,500 of the gain on his separate return only if Beth joins him in making his choice.

Example 4 — sale after divorce and remarriage. In 1996, Bill and Sally White were divorced. At that time they had their jointly owned home up for sale. Sally married Ken Brown in January 1997. In April 1997, Bill and Sally sold their home at a gain. Because Bill and Sally were not married to each other at the time they sold their home and they each met the tests to exclude gain, each can choose to exclude up to $125,000 gain based on the part of the home each owned. (See the *Example* under *Joint owners who are not married,* on page 30.)

Sally files a joint return with Ken and chooses to exclude up to $125,000 of her part of the gain. Ken must join Sally in her choice because he was her spouse at the time of sale. Bill files a single return and chooses to exclude up to $125,000 of his gain.

Example 5 — divorce after sale. Frank and Sheila Brown were married in 1990. In 1995, they sold their jointly owned home. Frank and Sheila met the age, ownership, and use tests, so they chose to exclude their gain of $70,000 on their joint return for that year. The Browns divorced in 1996.

In July 1997, Sheila married Mike Jones. Mike had sold his home in January 1997 when he was single. He met the age, ownership, and use tests at the time of sale. Mike can choose to exclude up to $125,000 gain on a separate or joint return. He can do this because Sheila (who already excluded gain) does not have to join in Mike's choice since he was single at the time he sold his home. In contrast, Sheila had to join Frank in choosing to exclude gain because they were married when they sold their home.

How To Make and Revoke a Choice To Exclude Gain

Under the rules explained in this chapter, you can exclude gain on the sale of your main home ***only once*** for sales after July 26, 1978.

For sales after May 6, 1997, you may be able to exclude gain under the rules explained in chapter 2.

Time to exclude gain. You can make or revoke a choice to exclude gain from a particular sale at any time before the ***latest*** of the following dates.

1) Three years from the due date of the return for the year of the sale.
2) Three years from the date you filed the return.
3) Two years from the date you paid the tax.

Period of disability. You may have longer to make or revoke your choice in some cases. This is because the 3-year and 2-year periods just described are suspended during any period when you cannot manage your finances due to a medically determinable physical or mental impairment that has lasted or can be expected to last for a continuous period of at least 12 months or to result in death. But there is no suspension for any period when your spouse or someone else was authorized to act for you.

How to make the choice. You can choose to exclude the gain even if you originally included it on your tax return for the year of the sale. You do so by filing an amended return (Form 1040X) for that year. You must send a filled-in Form 2119 or a statement with your amended return. The statement must say you choose to exclude from income the gain on the sale. It must also include the following information.

1) Your name, age, social security number, and marital status on the date of the sale. If the home was jointly owned, give this information for each owner.
2) The dates you bought and sold the home.
3) The amount realized and the adjusted basis of the property on the date of sale.
4) How long you were away from the home during the 5 years before the sale. Do not include vacation and other seasonal absences, even if you rented out the home during those absences.
5) Whether you or a joint owner ever chose to exclude gain on the sale of a home, and if you did, when and where you did so. If you revoked the choice, give the date you revoked it.

How to revoke the choice. You can revoke your choice to exclude gain by filing an amended return for the year of sale using Form 1040X. Attach a new completed Form 2119 and, if needed, a Schedule D (Form 1040). Send the forms to the Internal Revenue Service Center for the place where you live.

If you were married when you sold your home, your spouse who joined you in making the choice must join you in revoking it. If your spouse is deceased, his or her personal representative must join you in revoking the choice.

Example. On April 2, 1997, Joe Brown sold his separately owned home. Two months later his wife Joyce died, leaving a will that appointed the First National Bank of Hometown as her executor. When preparing his 1997 tax return, Joe had the bank join him in making the choice. If later he wants to revoke the choice, the bank must join him in revoking it.

Extension of assessment period. If you revoke your choice to exclude gain when less than a year is left in the assessment period (time for determining your correct tax) for the return on which the choice was made, you must agree to extend the assessment period. Before the end of the period, you must file a statement that the assessment period will not end until 1 year after the date the statement is filed. The assessment period normally ends on the latest of the dates shown earlier under *Time to exclude gain.*

Worksheet 4. **Sales for Which You Choose To Use the Rules in Chapter 3**

(See *Choosing To Use Rules in Chapter 3* on page 4.)

Part 1–Gain on Sale

1.	Selling price of home	**1.**	______
2.	Selling expenses	**2.**	______
3.	Subtract line 2 from line 1	**3.**	______
4.	Adjusted basis of home sold (from Worksheet 1, line 13)	**4.**	______
5.	Subtract line 4 from line 3. If zero or less, enter -0-. This is the **gain** on the sale	**5.**	______

Part 2–One-Time Exclusion of Gain for People Age 55 or Older

6.	If you choose to exclude gain, and you meet the age, ownership and use tests (see page 29), enter smaller of line 5 or $125,000 ($62,500 if married filing separate return). This is your **exclusion**	**6.**	______

Part 3–Taxable Gain and Adjusted Basis of New Home

7. If line 6 is blank, enter amount from line 5. Otherwise, subtract line 6 from line 5 . . . **7.** ______

- If line 7 is zero, stop. You do not have a taxable gain and will not report the sale on your return.
- If line 7 is more than zero and you have bought or built a new home, go to line 8.
- If neither of the above situations apply and you are reporting this sale on the installment method, stop here. The amount on line 7 is your taxable gain. See the instructions below.
- All others stop here and enter amount from line 7 on Schedule D (Form 1040).

8.	Fixing-up expenses	**8.**	______
9.	If line 6 is blank, enter amount from line 8. Otherwise, add lines 6 and 8	**9.**	______
10.	Subtract line 9 from line 3. This is your adjusted sales price	**10.**	______
11.	Enter the cost of your new home	**11.**	______
12.	Subtract line 11 from line 10. If zero or less, enter -0-	**12.**	______
13.	Enter the smaller of line 7 or line 12. This is your **taxable gain**	**13.**	______

- If line 13 is zero, go to line 14.
- If reporting on the installment method, see below, then go to line 14.
- All others report the amount from line 13 on Schedule D (Form 1040) and go to line 14.

14.	Subtract line 13 from line 7. This is your postponed gain	**14.**	______
15.	Subtract line 14 from line 11. This is the adjusted basis of your new home	**15.**	______

Installment Method—If you report the gain on Form 6252 using the installment method:

- Do not enter the gain from this worksheet on Schedule D. Your gain is reported on Form 6252.
- If you completed line 6 or line 14 of this worksheet, enter the total of those lines on line 15 of Form 6252.

Form **2119**

Department of the Treasury
Internal Revenue Service

Sale of Your Home

▶ Attach to Form 1040 for year of sale.

▶ See separate instructions. ▶ Please print or type.

OMB No. 1545-0072

1997

Attachment Sequence No. **20**

Your first name and initial. If a joint return, also give spouse's name and initial.	Last name	Your social security number
Frank G. and Evelyn M.	Smith	222 : 00 : 2222
If you are filing this form by itself and not with your tax return, see instructions on page 3. Present address (no., street, and apt. no., rural route, or P.O. box no. if mail is not delivered to street address)		Spouse's social security number 444 : 00 : 4444
City, town or post office, state, and ZIP code		

Part I Gain on Sale

Line	Description	Box	Amount
1	Date your former main home was sold. If sold after May 6, 1997, see page 3 ▶	1	5 / 1 / 97 (mo. day yr.)
2	Have you bought or built a new main home?		☑ Yes ☐ No
3	If any part of either main home was ever rented out or used for business, check here ▶ ☐ and see page 3.		
4	Selling price of home. Do not include personal property items you sold with your home	4	87,000
5	Expense of sale (see page 4)	5	5,200
6	Subtract line 5 from line 4	6	81,800
7	Adjusted basis of home sold (see page 4)	7	63,000
8	**Gain on sale.** Subtract line 7 from line 6. **If zero or less, stop** and attach this form to your return	8	18,800

- For sales **before May 7, 1997,** you must go to Part II or Part III, whichever applies. **But** if line 2 is "No," go to line 9.
- For sales **after May 6, 1997,** you must go to Part IV on the back to figure any exclusion. **But** if you qualify and elect to use the rules for sales before May 7, 1997, go to Part II or Part III, whichever applies.

9 If you haven't replaced your home, do you plan to do so within the **replacement period** (see page 1)? ☐ Yes ☐ No
- If line 9 is "Yes," stop here, attach this form to your return, and see **Additional filing requirements** on page 1.
- If line 9 is "No," you **must** go to Part II or Part III, whichever applies.

Part II One-Time Exclusion of Gain for People Age 55 or Older—By completing this part, you are electing to take the one-time exclusion (see page 2). If you are not electing to take the exclusion, go to Part III now.

Line	Description	Box	Amount
10	Who was age 55 or older on the date of sale? ☐ You ☐ Your spouse ☐ Both of you		
11	Did the person who was 55 or older own and use the property as his or her main home for a total of at least 3 years of the 5-year period before the sale? See page 2 for exceptions. If "No," go to Part III now ☐ Yes ☐ No		
12	At the time of sale, who owned the home? ☐ You ☐ Your spouse ☐ Both of you		
13	Social security number of spouse at the time of sale if you had a different spouse from the one above. If you were not married at the time of sale, enter "None" ▶	13	: :
14	**Exclusion.** Enter the **smaller** of line 8 or $125,000 ($62,500 if married filing separate return). Then, go to line 15	14	

Part III Adjusted Sales Price, Taxable Gain, and Adjusted Basis of New Home

Line	Description	Box	Amount
15	If line 14 is blank, enter the amount from line 8. Otherwise, subtract line 14 from line 8	15	18,800
	• If line 15 is zero, stop and attach this form to your return. • If line 15 is more than zero and line 2 is "Yes," go to line 16 now. • If you are reporting this sale on the installment method, stop and see page 4. • All others, stop and **enter the amount from line 15 on Schedule D, line 4 or line 11.**		
16	Fixing-up expenses (see page 4 for time limits)	16	500
17	If line 14 is blank, enter amount from line 16. Otherwise, add lines 14 and 16	17	500
18	**Adjusted sales price.** Subtract line 17 from line 6	18	81,300
19a	Date you moved into new home ▶ 4 / 20 / 99 **b** Cost of new home (see page 5)	19b	77,200
20	Subtract line 19b from line 18. If zero or less, enter -0-	20	4,100
21	**Taxable gain.** Enter the **smaller** of line 15 or line 20	21	4,100
	• If line 21 is zero, go to line 22 and attach this form to your return. • If you are reporting this sale on the installment method, see the line 15 instructions and go to line 22. • All others, **enter the amount from line 21 on Schedule D, line 4 or line 11,** and go to line 22.		
22	Postponed gain. Subtract line 21 from line 15	22	14,700
23	**Adjusted basis of new home.** Subtract line 22 from line 19b	23	62,500

For Paperwork Reduction Act Notice, see page 6 of instructions. Cat. No. 11710J Form **2119** (1997)

4.

Recapture of Federal Subsidy

If you financed your home under a federally subsidized program (loans from tax-exempt qualified mortgage bonds or loans with mortgage credit certificates), you may have to recapture all or part of the benefit you received from that program when you sell or otherwise dispose of your home. You recapture the benefit by increasing your federal income tax for the year of the sale. The postponement and exclusion of gain provisions discussed earlier in this publication do not apply to this recapture tax.

The recapture tax is figured on **Form 8828.** If you sell your home and your mortgage loan is subject to the recapture rules, you must file Form 8828 even if you do not owe a recapture tax.

Loans subject to recapture rules. The recapture of the subsidy applies to loans provided after 1990 that:

1) Came from the proceeds of qualified mortgage bonds issued after August 15, 1986, or
2) Were based on mortgage credit certificates issued after 1990.

The recapture also applies to assumptions of these loans.

Federal subsidy benefit. If you received a mortgage loan from the proceeds of a tax-exempt bond, you received the benefit of a lower interest rate than was customarily charged on other mortgage loans. If you received a mortgage credit certificate with your mortgage loan, you were able to reduce your federal income taxes by a mortgage interest tax credit. Both of these benefits are federal mortgage subsidies.

Sale or other disposition. The sale or other disposition of your home includes an exchange, involuntary conversion, or any other disposition.

For example, if you ***give away*** your home (other than to your spouse or ex-spouse incident to divorce), you are considered to have “sold” it. You figure your recapture tax as if you had sold your home for its fair market value on the date you gave it away.

When the recapture applies. The recapture of the federal mortgage subsidy applies only if you meet ***both*** of the following conditions.

1) You sell or otherwise dispose of your home:
   a) At a gain, and
   b) During the first 9 years after the date you closed your mortgage loan.
2) Your income for the year of disposition is more than that year's adjusted qualifying income for your family size for that year (related to the income requirements a person must meet to qualify for the federally subsidized program).

When recapture does not apply. The recapture does ***not*** apply if any of the following situations apply to you:

- Your mortgage loan was a qualified home improvement loan of not more than $15,000,
- The home is disposed of as a result of your death,
- You dispose of the home more than 9 years after the date you closed your mortgage loan,
- You transfer the home to your spouse, or to your former spouse incident to a divorce, where no gain is included in your income,
- You dispose of the home at a loss,
- Your home is destroyed by a casualty, and you repair it or replace it on its original site within 2 years after the end of the tax year when the destruction happened, or
- You refinance your mortgage loan (unless you later meet the conditions listed previously under *When the recapture applies).*

Notice of amounts. At or near the time of settlement of your mortgage loan, you should receive a notice that provides the federally subsidized amount and other information you will need to figure your recapture tax.

How to figure and report the recapture. See Form 8828 and its instructions for information on how to figure the recapture. Attach Form 8828 to your Form 1040.

5.

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.gov**. While visiting our web site, you can select:

- *Frequently Asked Tax Questions* (located under *Taxpayer Help & Ed)* to find answers to questions you may have.
- *Forms & Pubs* to download forms and publications or search for forms and publications by topic or keyword.
- *Fill-in Forms* (located under *Forms & Pubs)* to enter information while the form is displayed and then print the completed form.
- *Tax Info For You* to view Internal Revenue Bulletins published in the last few years.
- *Tax Regs in English* to search regulations and the Internal Revenue Code (under *United States Code (USC)).*
- *Digital Dispatch* and *IRS Local News Net* (both located under *Tax Info For Business)* to receive our electronic newsletters on hot tax issues and news.
- *Small Business Corner* (located under *Tax Info For Business)* to get information on starting and operating a small business.

You can also reach us with your computer using File Transfer Protocol at **ftp.irs.gov.**

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.

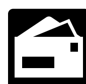
- *Ordering forms, instructions, and publications.* Call **1–800–829–3676** to order current and prior year forms, instructions, and publications.
- *Asking tax questions.* Call the IRS with your tax questions at **1–800–829–1040**.
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **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 within 10 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

Index

A
Abandonment 4
Address:
  Change of 1
Adjusted basis 8
Adjusted sales price 23
Amended return 22
Amount realized 3
Armed Forces 21
Assistance *(See* More information*)*

B
Basis 5
Business use of home 14, 23, 25, 30

C
Capital gains 28
Casualties 14, 15, 24, 30, 31
Change of address 1
Changed to rental property 23, 24
Closing costs 5, 25
Combat zone service 21
Community property 7
Condemned property 14, 15, 24, 30, 31
Construction 6
Cooperative apartment 6, 13
Cost as basis 5
Cost of new home 25

D
Deceased spouse 26, 30, 31
Depreciation 14
Divorced individuals:
  Divorce after sale 28
  Home received from spouse 7
  Home replaced by separate new homes 27
  Home transferred to spouse 4
  Main home 14

E
Example, illustrated 16
Examples, illustrated 28
Exclusion of gain:
  Sales before May 7, 1997 29
  Sales in 1998 10
Expatriates 15

F
Fair market value 6
Federal subsidy 36
Fixing-up expenses 23
Foreclosure 4
Form:
  1099–A 4
  1099–C 4
  1099–S 3
  2119 .... 27, 33
  4797 14
  8828 36
Free tax services 36

G
Gain on sale:
  Defined 4
  Exclusion of 10, 29
  Postponing 19
  When taxable 5
Gift 7, 26

H
Help *(See* More information*)*
Holding period 25
Home owned by one spouse 26
How to report 16, 27

I
Improvements 8
Individual taxpayer identification number 16
Individuals with disability 13, 30
Inheritance 7, 26
Installment sale 16, 28

L
Loss on sale 4, 5, 27

M
Main home:
  Changed to rental property 23, 24
  Defined 2
  More than one 3, 25
Married individuals:
  Basis of home received from spouse 7
  Community property 7
  Deceased spouse 14, 26, 30, 31
  Divorce after sale 28
  Home not jointly owned 31
  Home owned by one spouse 26
  Jointly owned home 4, 30
  Main home after divorce 14
  Outside U.S. 20
  Sales after May 6, 1997 14
  Separate homes 27
  Separate returns 31
  Spouse in Armed Forces 21, 22
  Surviving spouse, basis of home 7
  Title not held by either spouse 25
  Transfer of home to spouse 4
More information 36
More than one home 3, 25
Mortgage, seller-financed 16
Move, work related 25

N
New home 3, 24, 28

O
Old home:
  Business use of 23
  Casualties 24, 30
  Changed to rental property 23, 24
  Condemned 24, 30
  Not replaced 28
  Partly rental property 23
Ownership and use tests 12, 29

P
Partly used as home 14, 23, 25, 30
Payment by employer 3, 5
People outside the U.S. 20
Points 1, 5, 25
Postponing gain 19
Protective claim 22
Publications *(See* More information*)*

R
Received from spouse 7, 14
Recordkeeping 8
Rental property 14, 23, 24, 25
Repairs 8
Replacement period 20
Reporting the sale 16, 27
Repossession 4
Retirement home 25

S
Sales to related persons, exception 15
Second sale in replacement period 25
Seller-financed mortgage 16
Selling expenses 3
Selling price 3
Separate homes replaced by single home 27
Separate returns 4
Settlement fees 5, 25

Single home replaced by separate homes 27
Statute of limitations 28

T

Tax help *(See* More information*)*
Tax home 21
Taxes:
  Real estate 6, 19, 25
  Transfer 19
Title not held by you or spouse 25
Trade 7
Trading homes 4
Transfer to/from spouse 4, 7, 14
TTY/TDD information 36

■

Tax Publications for Individual Taxpayers

See *How To Get More Information* for a variety of ways to get publications, including by computer, phone, and mail.

General Guides

1 Your Rights as a Taxpayer
17 Your Federal Income Tax (For Individuals)
225 Farmer's Tax Guide
334 Tax Guide for Small Business
509 Tax Calendars for 2000
553 Highlights of 1999 Tax Changes
595 Tax Highlights for Commercial Fishermen
910 Guide to Free Tax Services

Specialized Publications

3 Armed Forces' Tax Guide
378 Fuel Tax Credits and Refunds
463 Travel, Entertainment, Gift, and Car Expenses
501 Exemptions, Standard Deduction, and Filing Information
502 Medical and Dental Expenses
503 Child and Dependent Care Expenses
504 Divorced or Separated Individuals
505 Tax Withholding and Estimated Tax
508 Tax Benefits for Work-Related Education
514 Foreign Tax Credit for Individuals
516 U.S. Government Civilian Employees Stationed Abroad
517 Social Security and Other Information for Members of the Clergy and Religious Workers
519 U.S. Tax Guide for Aliens
520 Scholarships and Fellowships
521 Moving Expenses
523 Selling Your Home
524 Credit for the Elderly or the Disabled
525 Taxable and Nontaxable Income
526 Charitable Contributions
527 Residential Rental Property
529 Miscellaneous Deductions
530 Tax Information for First-Time Homeowners
531 Reporting Tip Income
533 Self-Employment Tax
534 Depreciating Property Placed in Service Before 1987
537 Installment Sales
541 Partnerships
544 Sales and Other Dispositions of Assets
547 Casualties, Disasters, and Thefts (Business and Nonbusiness)
550 Investment Income and Expenses
551 Basis of Assets
552 Recordkeeping for Individuals
554 Older Americans' Tax Guide
555 Community Property
556 Examination of Returns, Appeal Rights, and Claims for Refund
559 Survivors, Executors, and Administrators
561 Determining the Value of Donated Property
564 Mutual Fund Distributions
570 Tax Guide for Individuals With Income From U.S. Possessions
575 Pension and Annuity Income
584 Casualty, Disaster, and Theft Loss Workbook (Personal-Use Property)
587 Business Use of Your Home (Including Use by Day-Care Providers)
590 Individual Retirement Arrangements (IRAs) (Including Roth IRAs and Education IRAs)
593 Tax Highlights for U.S. Citizens and Residents Going Abroad
594 Understanding the Collection Process
596 Earned Income Credit (EIC)
721 Tax Guide to U.S. Civil Service Retirement Benefits
901 U.S. Tax Treaties
907 Tax Highlights for Persons with Disabilities
908 Bankruptcy Tax Guide
911 Direct Sellers
915 Social Security and Equivalent Railroad Retirement Benefits
919 How Do I Adjust My Tax Withholding?
925 Passive Activity and At-Risk Rules
926 Household Employer's Tax Guide
929 Tax Rules for Children and Dependents
936 Home Mortgage Interest Deduction
946 How To Depreciate Property
947 Practice Before the IRS and Power of Attorney
950 Introduction to Estate and Gift Taxes
967 IRS Will Figure Your Tax
968 Tax Benefits for Adoption
970 Tax Benefits for Higher Education
971 Innocent Spouse Relief
972 Child Tax Credit
1542 Per Diem Rates
1544 Reporting Cash Payments of Over $10,000
1546 The Taxpayer Advocate Service of the IRS

Spanish Language Publications

1SP Derechos del Contribuyente
579SP Cómo Preparar la Declaración de Impuesto Federal
594SP Comprendiendo el Proceso de Cobro
596SP Crédito por Ingreso del Trabajo
850 English-Spanish Glossary of Words and Phrases Used in Publications Issued by the Internal Revenue Service
1544SP Informe de Pagos en Efectivo en Exceso de $10,000 (Recibidos en una Ocupación o Negocio)

Commonly Used Tax Forms

See *How To Get More Information* for a variety of ways to get forms, including by computer, fax, phone, and mail. For fax orders only, use the catalog numbers when ordering.

Form Number and Title	Catalog Number
1040 U.S. Individual Income Tax Return	11320
Sch A & B Itemized Deductions & Interest and Ordinary Dividends	11330
Sch C Profit or Loss From Business	11334
Sch C-EZ Net Profit From Business	14374
Sch D Capital Gains and Losses	11338
Sch D-1 Continuation Sheet for Schedule D	10424
Sch E Supplemental Income and Loss	11344
Sch EIC Earned Income Credit	13339
Sch F Profit or Loss From Farming	11346
Sch H Household Employment Taxes	12187
Sch J Farm Income Averaging	25513
Sch R Credit for the Elderly or the Disabled	11359
Sch SE Self-Employment Tax	11358
1040A U.S. Individual Income Tax Return	11327
Sch 1 Interest and Ordinary Dividends for Form 1040A Filers	12075
Sch 2 Child and Dependent Care Expenses for Form 1040A Filers	10749
Sch 3 Credit for the Elderly or the Disabled for Form 1040A Filers	12064
1040EZ Income Tax Return for Single and Joint Filers With No Dependents	11329
1040-ES Estimated Tax for Individuals	11340
1040X Amended U.S. Individual Income Tax Return	11360
2106 Employee Business Expenses	11700
2106-EZ Unreimbursed Employee Business Expenses	20604
2210 Underpayment of Estimated Tax by Individuals, Estates, and Trusts	11744
2441 Child and Dependent Care Expenses	11862
2848 Power of Attorney and Declaration of Representative	11980
3903 Moving Expenses	12490
4562 Depreciation and Amortization	12906
4868 Application for Automatic Extension of Time To File U.S. Individual Income Tax Return	13141
4952 Investment Interest Expense Deduction	13177
5329 Additional Taxes Attributable to IRAs, Other Qualified Retirement Plans, Annuities, Modified Endowment Contracts, and MSAs	13329
6251 Alternative Minimum Tax–Individuals	13600
8283 Noncash Charitable Contributions	62299
8582 Passive Activity Loss Limitations	63704
8606 Nondeductible IRAs	63966
8812 Additional Child Tax Credit	10644
8822 Change of Address	12081
8829 Expenses for Business Use of Your Home	13232
8863 Education Credits	25379