

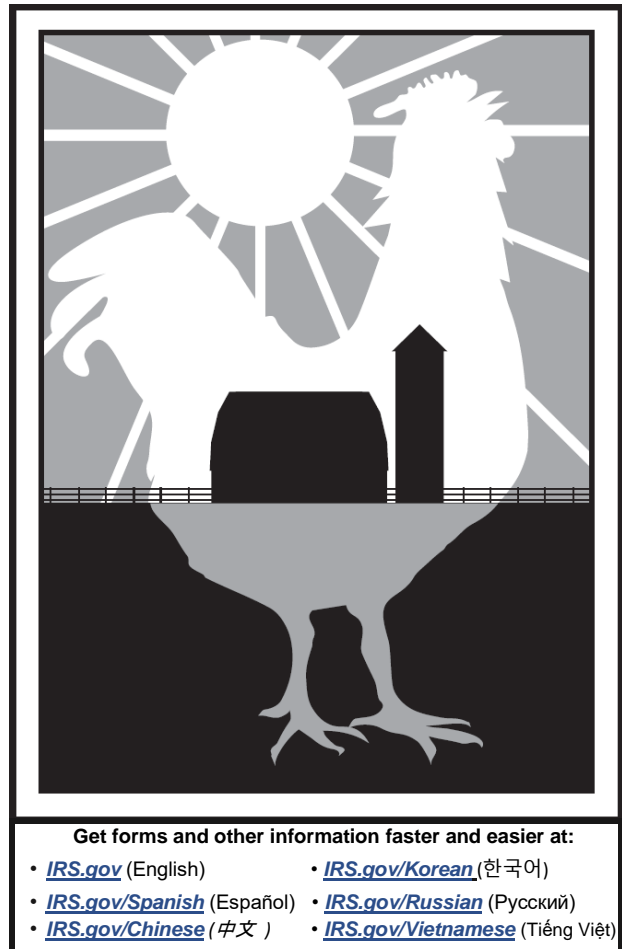
Publication 225

Farmers Tax Guide

For use in preparing

2024 Returns

Volume 7 of 11



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Successor. Converted wetland or highly erodible cropland is also land held by any person whose basis in the land is figured by reference to the adjusted basis of a person in whose hands the property was converted wetland or highly erodible cropland.

Timber

Standing timber you held as investment property is a capital asset. Gain or loss from its sale is capital gain or loss reported on Form 8949 and Schedule D (Form 1040), as applicable. If you held the timber primarily for sale to customers, it is not a capital asset. Gain or loss on its sale is ordinary business income or loss. It is reported on Schedule F, line 1 (if purchased timber) or line 2 (if raised timber).

Farmers who cut timber on their land and sell it as logs, firewood, or pulpwood usually have no cost or other basis for that timber if no allocation was made at the time of

acquisition. Amounts realized from these sales, and the expenses incurred in cutting, hauling, etc., are ordinary farm income and expenses reported on Schedule F.

Different rules apply if you owned the timber longer than 1 year and elect to treat timber cutting as a sale or exchange or you enter into a cutting contract, discussed below.

Timber considered cut. Timber is considered cut on the date when, in the ordinary course of business, the quantity of felled timber is first definitely determined. This is true whether the timber is cut under contract or whether you cut it yourself.

Christmas trees. Evergreen trees, such as Christmas trees, that are more than 6 years old when severed from their roots and sold for ornamental purposes are included in the term "timber." They qualify for both rules discussed below.

Election to treat cutting as a sale or exchange. Under the general rule, the cutting of timber results in no gain or loss. It is not until a sale or exchange occurs that gain or loss is realized. But if you owned or had a contractual right to cut timber, you can elect to treat the cutting of timber as a section 1231 transaction in the year it is cut. Even though the cut timber is not actually sold or exchanged, you report your gain or loss on the cutting for the year the timber is cut. Any later sale results in ordinary business income or loss. See the example below. To elect this treatment, you must:

1. Own or hold a contractual right to cut the timber for a period of more than 1 year before it is cut, and
2. Cut the timber for sale or use in your trade or business.

Making the election. You make the election on your return for the year the cutting takes place by including in income the gain or loss

on the cutting and including a computation of your gain or loss. You do not have to make the election in the first year you cut timber. You can make it in any year to which the election would apply. If the timber is partnership property, the election is made on the partnership return. This election cannot be made on an amended return.

Once you have made the election, it remains in effect for all later years unless you revoke it.

Election under section 631(a) may be revoked. If you previously elected for any tax year ending before October 23, 2004, to treat the cutting of timber as a sale or exchange under section 631(a), you may revoke this election without the consent of the IRS for any tax year ending after October 22, 2004. The prior election (and revocation) is disregarded for purposes of making a subsequent election. See Form T (Timber),

Forest Activities Schedule, for more information.

Gain or loss. Your gain or loss on the cutting of standing timber is the difference between its adjusted basis for depletion and its FMV on the first day of your tax year in which it is cut. The FMV becomes your basis in the cut timber, and a later sale of the cut timber, including any by-product or tree tops, will result in ordinary business income or loss.

Your adjusted basis for depletion of cut timber is based on the number of units (board feet, log scale, or other units) of timber cut during the tax year and considered to be sold or exchanged. Your adjusted basis for depletion is also based on the depletion unit of timber in the account used for the cut timber, and should be figured in the same manner as shown in section 611 and Regulations section 1.611-3.

Depletion of timber is discussed in chapter 7.

Example. In April 2024, you owned 4,000 MBF (1,000 board feet) of standing timber longer than 1 year. It had an adjusted basis for depletion of \$40 per MBF. You are a calendar year taxpayer. On January 1, 2024, the timber had an FMV of \$350 per MBF. It was cut in April for sale. On your 2024 tax return, you elect to treat the cutting of the timber as a sale or exchange. You report the difference between the FMV and your adjusted basis for depletion as a gain. This amount is reported on Form 4797 along with your other section 1231 gains and losses to figure whether it is treated as a capital gain or as ordinary gain. You figure your gain as follows.

FMV of timber January 1, 2024	\$1,400,000
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Minus: Adjusted basis for depletion	<u>160,000</u>
-------------------------------------	----------------

Section 1231 gain	<u>\$1,240,000</u>
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Outright sales of timber. Outright sales of timber by landowners qualify for capital gains treatment using rules similar to the rules for certain disposal of timber under a contract with retained economic interest (defined later). However, for outright sales, the date of disposal is not deemed to be the date the timber is cut because the landowner can elect to treat the payment date as the date of disposal (see *Date of disposal*, later).

Cutting contract. You must treat the disposal of standing timber under a cutting contract as a section 1231 transaction if all the following apply to you.

- You are the owner of the timber.
- You held the timber longer than 1 year before its disposal.
- You kept an economic interest in the timber.

You have kept an economic interest in standing timber if, under the cutting contract, the expected return on your investment is conditioned on the cutting of the timber.

The difference between the amount realized from the disposal of the timber and its adjusted basis for depletion is treated as gain or loss on its sale. Include this amount on Form 4797 along with your other section 1231 gains or losses.

Date of disposal. The date of disposal is the date the timber is cut. However, for outright sales by landowners or if you receive payment under the contract before the timber is cut, you can elect to treat the date of payment as the date of disposal.

This election applies only to figure the holding period of the timber. It has no effect on the time for reporting gain or loss (generally when the timber is sold or exchanged).

To make this election, attach a statement to the tax return filed by the due date (including extensions) for the year payment is received.

The statement must identify the advance payments subject to the election and the contract under which they were made.

If you timely filed your return for the year you received payment without making the election, you can still make the election by filing an amended return within 6 months after the due date for that year's return (excluding extensions). Attach the statement to the amended return and enter "Filed pursuant to section 301.9100-2" at the top of the statement. File the amended return at the same address the original return was filed.

Owner. An owner is any person who owns an interest in the timber, including a sublessor and the holder of a contract to cut the timber. You own an interest in timber if you have the right to cut it for sale on your own account or for use in your business.

Tree stumps. Tree stumps are a capital asset if they are on land held by an investor who is not in the timber or stump business as a buyer, seller, or processor. Gain from the sale of stumps sold in one lot by such a holder is taxed as a capital gain. However, tree stumps held by timber operators after the saleable standing timber was cut and removed from the land are considered by-products. Gain from the sale of stumps in lots or tonnage by such operators is taxed as ordinary income.

See Form T (Timber) and its separate instructions for more information about dispositions of timber.

Sale of a Farm

The sale of your farm may involve the sale of both nonbusiness property (your home) and business property (the land and buildings used in the farm operation and perhaps machinery and livestock). If any gain from

the sale includes a gain from the sale of your home, you may be allowed to exclude the gain on your home. For more information, see Pub. 523.

The gain on the sale of your business property is taxable. A loss on the sale of your business property to an unrelated person is deducted as an ordinary loss. Your taxable gain or loss on the sale of property used in your farm business is taxed under the rules for section 1231 transactions. See chapter 9. Losses from personal-use property, other than casualty or theft losses, are not deductible. If you receive payments for your farm in installments, certain gains may be eligible to be taxed over the period of years the payments are received. See chapter 10 for information about installment sales.

When you sell your farm, the gain or loss on each asset is figured separately. The tax treatment of gain or loss on the sale of each asset is determined by the classification of

the asset. Each of the assets sold must be classified as one of the following.

- Capital asset held 1 year or less.
- Capital asset held longer than 1 year.
- Property (including real estate) used in your business and held 1 year or less (including draft, breeding, dairy, and sporting animals held less than the holding periods discussed earlier under Livestock).
- Property (including real estate) used in your business and held longer than 1 year (including only draft, breeding, dairy, and sporting animals held for the holding periods discussed earlier).
- Property held primarily for sale or which is of the kind that would be included in inventory if on hand at the end of your tax year.

Allocation of consideration paid for a farm. The sale of a farm for a lump sum is considered a sale of each individual asset rather than a single asset. If the group of assets sold constitutes a trade or business, the residual method must be used. This method determines gain or loss from the transfer of each asset. It also determines the buyer's basis in the business assets. For more information, see *Sale of a Business* in chapter 2 of Pub. 544.

Property used in farm operation. The rules for excluding the gain on the sale of your home, described later under *Sale of your home*, do not apply to the property used for your farming business. Recognized gains and losses on business property must be reported on your return for the year of the sale. If the property was held longer than 1 year, it may qualify for section 1231 treatment (see chapter 9).

Example. You sell your farm, including your main home, which you have owned since December 2006. You realize gain on the sale as follows.

	Farm With Home	Home Only	Farm Without Home
Selling price	\$382,000	\$158,000	\$224,000
Cost (or other basis)	240,000	110,000	130,000
Gain	\$142,000	\$48,000	\$94,000

You must report the \$94,000 gain from the sale of the property used in your farm business. All or a part of that gain may have to be reported as ordinary income from the recapture of depreciation or soil and water

conservation expenses. Treat the balance as section 1231 gain.

The \$48,000 gain from the sale of your home is not taxable if you meet the requirements explained later under *Sale of your home*.

Partial sale. If you sell only part of your farm, you must report any recognized gain or loss on the sale of that part on your tax return for the year of the sale. You cannot wait until you have sold enough of the farm to recover its entire cost before reporting gain or loss. For a detailed discussion on installment sales, see Pub. 544.

Adjusted basis of the part sold. This is the properly allocated part of your original cost or other basis of the entire farm plus or minus necessary adjustments for improvements, depreciation, etc., on the part sold. If your home is on the farm, you must properly adjust the basis to exclude those costs from your farm asset costs, as discussed later under *Sale of your home*.

Example. You bought a 200-acre farm for \$700,000. The farm included land and buildings. The purchase contract designated \$600,000 of the purchase price to the land. You later sold 20 acres of land on which you had installed a fence. Your adjusted basis for the part of your farm sold is \$60,000 ($\frac{1}{10}$ of \$600,000), plus any unrecovered cost (cost not depreciated) of the fence on the 20 acres at the time of sale. Use this amount to determine your gain or loss on the sale of the 20 acres.

Assessed values for local property taxes.

If you paid a flat sum for the entire farm and no other facts are available for properly allocating your original cost or other basis between the land and the buildings, you can use the assessed values for local property taxes for the year of purchase to allocate the costs.

Worksheet 8-1. **Worksheet for Foreclosures
and Repossessions**

Keep for Your Records



Part 1. Use Part 1 to figure your ordinary income from the cancellation of debt upon foreclosure or repossession. Complete this part only if you were personally liable for the debt. Otherwise, go to Part 2.	
1. Enter the amount of outstanding debt immediately before the transfer of property reduced by any amount for which you remain personally liable after the transfer of property	_____
2. Enter the FMV of the transferred property	_____
3. Ordinary income from cancellation of debt upon foreclosure or repossession.* Subtract line 2 from line 1. If zero or less, enter -0-	=====
Part 2. Figure your gain or loss from foreclosure or repossession.	
4. If you completed Part 1, enter the smaller of line 1 or line 2. If you did not complete Part 1, enter the outstanding debt immediately before the transfer of property	_____
5. Enter any proceeds you received from the foreclosure sale	_____
6. Add lines 4 and 5	_____
7. Enter the adjusted basis of the transferred property	_____
8. Gain or loss from foreclosure or repossession. Subtract line 7 from line 6	=====

* The income may not be taxable. See [Cancellation of debt](#), later.

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Example. Assume that in the preceding example there was no breakdown of the \$700,000 purchase price between land and buildings. However, in the year of purchase, local taxes on the entire property were based on assessed valuations of \$420,000 for land and \$140,000 for improvements, or a total of \$560,000. The assessed valuation of the land is $\frac{3}{4}$ (75%) of the total assessed valuation. Multiply the \$700,000 total purchase price by 75% to figure basis of \$525,000 for the 200 acres of land. The unadjusted basis of the 20 acres you sold would then be \$52,500 ($\frac{1}{10}$ of \$525,000).

Sale of your home. Your home is a capital asset and not property used in the trade or business of farming. If you sell a farm that includes a house you and your family occupy, you must determine the part of the selling price and the part of the cost or other basis allocable to your home. Your home includes the immediate surroundings and outbuildings

relating to it that are not used for business purposes.

If you use part of your home for business, you must make an appropriate adjustment to the basis for depreciation allowed or allowable. For more information on basis, see chapter 6.

More information. For more information on selling your home, see Pub. 523.

Gain from condemnation. If you have a gain from a condemnation or sale of your home under threat of condemnation, you may use the preceding rules for excluding the gain, rather than the rules discussed under *Postponing Gain* in chapter 11. However, any gain that cannot be excluded (because it is more than the limit) may be postponed under the rules discussed under *Postponing Gain* in chapter 11.

Foreclosure or Repossession

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

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



You can use Worksheet 8-1 to figure your gain or loss from a foreclosure or repossession.

Amount realized on a nonrecourse debt.

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

Example 1. You paid \$200,000 for land used in your farming business. You paid \$15,000 down and borrowed the remaining \$185,000 from a bank. You are not personally liable for the loan (nonrecourse debt), but pledge the land as security. The bank foreclosed on the loan 2 years after you stopped making payments. When the bank foreclosed, the balance due on the loan was \$180,000 and the FMV of the land was \$170,000. The

amount you realized on the foreclosure was \$180,000, the debt canceled by the foreclosure. You figure your gain or loss on Form 4797, Part I, by comparing the amount realized (\$180,000) with your adjusted basis (\$200,000). You have a \$20,000 deductible loss.

Example 2. Assume the same facts as in *Example 1*, except the FMV of the land was \$210,000. The result is the same. The amount you realized on the foreclosure is \$180,000, the debt canceled by the foreclosure. Because your adjusted basis is \$200,000, you have a deductible loss of \$20,000, which you report on Form 4797, Part I.

Amount realized on a recourse debt. If you are personally liable for the debt (recourse debt), the amount realized on the foreclosure or repossession includes the lesser of:

- The outstanding debt immediately before the transfer reduced by any amount for which you remain personally liable immediately after the transfer, or
- The FMV of the transferred property.

You are treated as receiving ordinary income from the canceled debt for the part of the debt that is more than the FMV. The amount realized does not include the canceled debt that is your income from cancellation of debt. See Cancellation of debt, later.

Example 3. Assume the same facts as in *Example 1* earlier, except you are personally liable for the loan (recourse debt). In this case, the amount you realize is \$170,000. This is the canceled debt (\$180,000) up to the FMV of the land (\$170,000). You figure your gain or loss on the foreclosure by comparing the amount realized (\$170,000) with your adjusted basis (\$200,000). You have a \$30,000 deductible loss, which you figure on Form 4797, Part I. You are also

treated as receiving ordinary income from cancellation of debt. That income is \$10,000 (\$180,000 – \$170,000). This is the part of the canceled debt not included in the amount realized. You report this as other income on Schedule F, line 8.

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

Cancellation of debt. If property that is repossessed or foreclosed upon secures a debt for which you are personally liable (recourse debt), you must generally report as ordinary income the amount by which the canceled debt is more than the FMV of the property. This income is separate from any gain or loss realized from the foreclosure or

repossession. Report the income from cancellation of a business debt on Schedule F, line 8. Report the income from cancellation of a nonbusiness debt as miscellaneous income on Form 1040 or Form 1040-SR.



You can use Worksheet 8-1 to figure your income from cancellation of debt.

However, income from cancellation of debt is not taxed in certain situations. See Cancellation of Debt in chapter 3.

Abandonment

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

Business or investment property. Loss from abandonment of business or investment property is deductible as a loss. Loss from

abandonment of business or investment property that is not treated as a sale or exchange is generally an ordinary loss. If your adjusted basis is more than the amount you realize (if any), then you have a loss. If the amount you realize (if any) is more than your adjusted basis, then you have a gain. This rule also applies to leasehold improvements the lessor made for the lessee. However, if the property is foreclosed on or repossessed in lieu of abandonment, gain or loss is figured as discussed earlier under Foreclosure or Repossession.

If the abandoned property is secured by debt, special rules apply. The tax consequences of abandonment of property that secures a debt depend on whether you are personally liable for the debt (recourse debt) or were not personally liable for the debt (nonrecourse debt). For more information, see chapter 3 of Pub. 4681, Canceled Debts, Foreclosures, Repossessions, and Abandonments.

The abandonment loss is deducted in the tax year in which the loss is sustained. Report the loss on Form 4797, Part II, line 10.

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

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

However, income from cancellation of debt is not taxed in certain circumstances. See Cancellation of debt, earlier, under Foreclosure or Repossession.

Forms 1099-A and 1099-C. A lender who acquires an interest in your property in a foreclosure, repossession, or abandonment should send you Form 1099-A showing the information you need to figure your loss from the foreclosure, repossession, or abandonment. However, if the lender cancels part of your debt and the lender must file Form 1099-C, the lender may include the information about the foreclosure, repossession, or abandonment on that form instead of Form 1099-A. The lender must file Form 1099-C and send you a copy if the canceled debt is \$600 or more and the lender is a financial institution, credit union, or federal government agency, or any organization that has a significant trade or business of lending money. For foreclosures, repossessions, abandonments of property, and debt cancellations occurring in 2024, these forms should be sent to you by January 31, 2025.

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9.

Dispositions of Property Used in Farming

Introduction

When you dispose of property used in your farm business, your taxable gain or loss is usually treated as ordinary income or capital gain (under the rules for section 1231 transactions). Ordinary income is taxed at the same rate as wages and interest. Capital gain is generally taxed at lower rates.

When you dispose of depreciable property (section 1245 property or section 1250 property) at a gain, you may have to recognize all or part of the gain as ordinary income under the depreciation recapture rules. Any gain remaining after applying the depreciation recapture rules is a section 1231 gain, which may be taxed as a capital gain. Similar rules apply to the sale of property on

which soil and water conservation expenses have been deducted or government cost-sharing payments have been received.

Gains and losses from property used in farming are reported on Form 4797, Sales of Business Property. Table 9-1 contains examples of items reported on Form 4797 and refers to the part of that form on which they should first be reported.

Topics

This chapter discusses:

- Section 1231 gains and losses
- Depreciation recapture
- Other gains

Useful Items

You may want to see:

Publication

- **544** Sales and Other Dispositions of Assets

Form (and Instructions)

- **4797** Sales of Business Property

See [How To Get Tax Help](#) for information about getting publications and forms.

Section 1231 Gains and Losses

Section 1231 gains and losses are the taxable gains and losses from section 1231 transactions (explained below). Their treatment as ordinary income or loss or capital gains depends on whether you have a net gain or a net loss from all of your section 1231 transactions in the tax year.

If you have a gain from a section 1231 transaction, first determine whether any of the gain is ordinary income under the depreciation (or other) recapture rules explained later. Do not take that gain into account as section 1231 gain. Only gain in

excess of the recapture amount is considered section 1231 gain. See Treatment as ordinary or capital, later.

Section 1231 transactions. Section 1231 transactions are sales and exchanges of real or depreciable property used in trade or business and held the required holding period (based on type of asset, as discussed below). Gain or loss on the following transactions is subject to section 1231 treatment.

- ***Sale or exchange of cattle and horses.***

The cattle and horses must be held for draft, breeding, dairy, or sporting purposes and held for 24 months or longer.

- ***Sale or exchange of other livestock.***

This livestock must be held for draft, breeding, dairy, or sporting purposes and held for 12 months or longer. Other livestock includes hogs, mules, sheep, goats, donkeys, and other fur-bearing

animals. Other livestock does not include poultry.

- ***Sale or exchange of depreciable real property or personal property.*** This property must be used in your business and held longer than 1 year. Generally, property held for the production of rents or royalties is considered to be used in a trade or business. This property must also be either real property or is of a kind that is subject to depreciation under section 167 of the Internal Revenue Code. Examples of depreciable personal property include farm machinery and trucks. It also includes amortizable section 197 intangibles.
- ***Sale or exchange of real estate.*** This property must be used in your business and held longer than 1 year. Examples include your farm or ranch (including barns and sheds).

- ***Sale or exchange of unharvested crops.*** The crop and land must be sold, exchanged, or involuntarily converted at the same time and to the same person, and the land must have been held longer than 1 year. You cannot keep any right or option to reacquire the land directly or indirectly (other than a right customarily incident to a mortgage or other security transaction). Growing crops sold with a leasehold on the land, even if sold to the same person in a single transaction, is not considered a section 1231 transaction.

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- ***Distributive share of partnership gains and losses.*** Your distributive share must be from the sale or exchange of property listed above and held by the partnership for longer than 1 year (or for the required period for certain livestock). You will receive Schedule K-1 (Form 1065)

showing the appropriate classification of any gains or losses distributed to you.

- ***Cutting or disposal of timber.*** Special rules apply if you owned the timber longer than 1 year and elect to treat timber cutting as a sale or exchange, or you enter into a cutting contract, as described in chapter 8 under *Timber*.
- ***Condemnation.*** The condemned property (defined in chapter 11) must have been held longer than 1 year. It must be business property or a capital asset held in connection with a trade or business or a transaction entered into for profit, such as investment property. It cannot be property held for personal use.
- ***Casualty or theft.*** The casualty or theft must have affected business property, property held for the production of rents or royalties, or investment property (such as notes and bonds). You must have held the property longer than the required

holding period. However, if your casualty or theft losses are more than your casualty or theft gains, the net casualty or theft loss is fully deductible and is not combined with other section 1231 transactions in the section 1231 computation. Section 1231 does not apply to personal casualty gains and losses. See chapter 11 for information on how to treat those gains and losses.



If the property is not held for the required holding period, the transaction is not subject to section 1231 treatment, and any gain or loss is ordinary income reported in Part II of Form 4797. See Table 9-1.

Treatment as ordinary or capital. To determine the treatment of section 1231 gains and losses, combine all of your section 1231 gains and losses for the year.

- If you have a net section 1231 loss, it is an ordinary loss.

- If you have a net section 1231 gain, it is ordinary income up to your nonrecaptured section 1231 losses from previous years, explained next. The rest, if any, is long-term capital gain.

Nonrecaptured section 1231 losses. Your nonrecaptured section 1231 losses are your net section 1231 losses for the previous 5 years that have not been applied against a net section 1231 gain. Therefore, if in any of your 5 preceding tax years you had section 1231 losses, a net gain for the current year from the sale of section 1231 assets is ordinary gain to the extent of your prior losses. These losses are applied against your net section 1231 gain beginning with the earliest loss in the 5-year period.

Example. In 2024, you have a \$20,000 net section 1231 gain. To figure how much you have to report as ordinary income and long-term capital gain, you must first determine your section 1231 gains and losses from the previous 5-year period. From 2019 through 2023, you had the following section 1231 gains and losses

Table 9-1. Where To First Report Certain Items on Form 4797

Type of property		Held 1 year or less	Held more than 1 year
1 Depreciable trade or business property: a Sold or exchanged at a gain b Sold or exchanged at a loss		Part II	Part III (1245, 1250)
		Part II	Part I
	2 Farmland held less than 10 years for which soil or water expenses were deducted: a Sold at a gain b Sold at a loss	Part II	Part III (1252)
		Part II	Part I
3 All other farmland used in a trade or business		Part II	Part I
4 Disposition of cost-sharing payment property described in section 126		Part II	Part III (1255)
5 Cattle and horses used in a trade or business for draft, breeding, dairy, or sporting purposes: a Sold at a gain b Sold at a loss c Raised cattle and horses sold at a gain		Held less than 24 mos.	Held 24 mos. or more
		Part II	Part III (1245)
		Part II	Part I
		Part II	Part I
6 Livestock other than cattle and horses used in a trade or business for draft, breeding, dairy, or sporting purposes: a Sold at a gain b Sold at a loss c Raised livestock sold at a gain		Held less than 12 mos.	Held 12 mos. or more
		Part II	Part III (1245)
		Part II	Part I
		Part II	Part I
7 Real or tangible trade or business property which was deducted under the de minimis safe harbor		Held 1 year or less	Held more than 1 year
		Part II	Part II

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Year	Amount
2019	-0-
2020	-0-
2021	(\$25,000)
2022	-0-
2023	\$18,000

You used this information to figure how to report your net section 1231 gain for 2024 as shown below.

- 1.** Net section 1231 gain (2024) \$20,000
- 2.** Net section 1231 loss (2021) (\$25,000)

- 3. Net section 1231
gain (2023) \$18,000
- 4. Remaining net
section 1231 loss
from prior 5 years (\$7,000)
- 5. Gain treated as
ordinary income \$7,000
- 6. **Gain treated as
long-term
capital gain** **(\$13,000)**

Your remaining net section 1231 loss from 2021 is completely recaptured in 2024.

Property held for sale to customers. A sale, exchange, or involuntary conversion of property held mainly for sale to customers is not a section 1231 transaction. If you will get back all, or nearly all, of your investment in the property by selling it rather than by using

it up in your business, it is property held mainly for sale to customers.

Property deducted under the de minimis safe harbor for tangible property. If you deducted the cost of a property under the de minimis safe harbor for tangible property (currently \$2,500 or less, or \$5,000 or less, if you have an applicable financial statement), then upon its sale or disposition, this property is not treated as a capital asset or as property used in the trade or business under section 1231. Generally, any gain on the disposition of this property is treated as ordinary income reported on Part II of Form 4797.

Depreciation Recapture

If you dispose of depreciable property (section 1245 or section 1250 property) or amortizable property at a gain, you may have to treat all or part of the gain (even if it is otherwise nontaxable) as ordinary income.

Any remaining gain is section 1231 gain (discussed earlier).



To figure any gain that must be reported as ordinary income, you must keep permanent records of the facts necessary to figure the depreciation or amortization allowed or allowable on your property. For more information on depreciation recapture, see chapter 3 of Pub. 544. Also see Pub. 946.

Section 1245 Property

A gain on the disposition of section 1245 property is treated as ordinary income to the extent of depreciation allowed or allowable. Any recognized gain that is more than the part that is ordinary income is a section 1231 gain.

Section 1245 property includes any property that is or has been subject to an allowance for depreciation or amortization and that is any of the following types of property.

1. Personal property (either tangible or intangible).
2. Other tangible property (except buildings and their structural components) used as any of the following. See Buildings and structural components, later.
 - a. An integral part of manufacturing, production, or extraction, or of furnishing certain services.
 - b. A research facility in any of the activities in (a).
 - c. A facility in any of the activities in (a) above, for the bulk storage of fungible commodities (discussed later).
3. Where applicable, that part of real property (not included in (2)) with an adjusted basis reduced by (but not limited to) the following.

- a. Amortization of certified pollution control facilities.
 - b. The section 179 expense deduction.
 - c. Deduction for clean-fuel vehicles and certain refueling property.
 - d. Expenditures to remove architectural and transportation barriers to the handicapped and elderly.
 - e. Certain reforestation expenditures (as described under *Reforestation Costs* in chapter 7).
- 4. Single-purpose agricultural (livestock) or horticultural structures.
 - 5. Storage facilities (except buildings and their structural components) used in distributing petroleum or any primary product of petroleum.

Buildings and structural components.

Section 1245 property does not include buildings and structural components. The term "building" includes a house, barn, warehouse, or garage. The term "structural component" includes walls, floors, windows, doors, central air conditioning systems, light fixtures, etc.

Do not treat a structure that is essentially machinery or equipment as a building or structural component. Also, do not treat a structure that houses property used as an integral part of an activity as a building or structural component if the structure's use is so closely related to the property's use that the structure can be expected to be replaced when the property it initially houses is replaced.

The fact that the structure is specially designed to withstand the stress and other demands of the property and cannot be used economically for other purposes indicates it is

closely related to the use of the property it houses. Structures such as oil and gas storage tanks, grain storage bins, and silos are not treated as buildings, but as section 1245 property.

Facility for bulk storage of fungible commodities. This is a facility used mainly for the bulk storage of fungible commodities. Bulk storage means storage of a commodity in a large mass before it is used. For example, if a facility is used to store oranges that have been sorted and boxed, it is not used for bulk storage. To be fungible, a commodity must be such that each of its parts is essentially interchangeable, and each of its parts is indistinguishable from another part.

Gain Treated as Ordinary Income

The gain treated as ordinary income on the sale, exchange, or involuntary conversion of section 1245 property, including a sale and

leaseback transaction, is the lesser of the following amounts.

1. The depreciation (which includes any section 179 deduction claimed) and amortization allowed or allowable on the property.
2. The gain realized on the disposition (the amount realized from the disposition minus the adjusted basis of the property).

See chapter 3 of Pub. 544 for more information on dispositions of section 1245 property.

Use Part III of Form 4797 to figure the ordinary income part of the gain.

Depreciation claimed on other property or claimed by other taxpayers.

Depreciation and amortization include the amounts you claimed on the section 1245 property as well as the following depreciation and amortization amounts.

- Amounts you claimed on property you exchanged for, or converted to, your section 1245 property in an applicable like-kind exchange or involuntary conversion. For details on exchanges of property that are not taxable, see *Like-Kind Exchanges* in chapter 8.
- Amounts a previous owner of the section 1245 property claimed if your basis is determined with reference to that person's adjusted basis (for example, the donor's depreciation deductions on property you received as a gift).

Depreciation and amortization.

Depreciation and amortization deductions that must be recaptured as ordinary income include (but are not limited to) the following items. See *Depreciation Recapture* in chapter 3 of Pub. 544 for more details.

1. Ordinary depreciation deductions.

2. The section 179 expense deduction (see chapter 7).
3. Any special depreciation allowance.
4. Amortization deductions for any of the following costs.
 - a. Acquiring a lease.
 - b. Lessee improvements.
 - c. Pollution control facilities.
 - d. Reforestation expenses.
 - e. Section 197 intangibles.
 - f. Qualified disaster expenses.
 - g. Franchises, trademarks, and trade names acquired before August 11, 1993.

Example. You file your returns on a calendar year basis. In February 2022, you bought and placed in service for 100% use in your farming business a light-duty truck (5-year property) that cost \$30,000. You used the

half-year convention and your MACRS deductions for the truck were \$6,000 in 2022 and \$9,600 in 2023. You did not claim the section 179 expense deduction for the truck. You sold it in May 2024 for \$21,000. The MACRS deduction in 2024, the year of sale, is \$2,880 ($\frac{1}{2}$ of \$5,760). Figure the gain treated as ordinary income as follows.

1.	Amount realized	\$21,000
2.	Cost (February 2022)	\$30,000
3.	Depreciation allowed or allowable (MACRS deductions: \$6,000 + \$9,600 + \$2,880)	<u>18,480</u>
4.	Adjusted basis (subtract line 3 from line 2)	<u>\$11,520</u>

5. Gain realized (subtract
line 4 from line 1) \$9,480

**6. Gain treated as
ordinary income
(lesser of line 3 or
line 5) \$9,480**

Depreciation allowed or allowable. You generally use the greater of the depreciation allowed or allowable when figuring the part of gain to report as ordinary income. If, in prior years, you have consistently taken proper deductions under one method, the amount allowed for your prior years will not be increased even though a greater amount would have been allowed under another proper method. If you did not take any deductions in prior years for depreciation, your adjustments to basis for depreciation allowable are figured by using the straight line method. This treatment applies only when figuring what part of the gain is treated

as ordinary income under the rules for section 1245 depreciation recapture. For more information on depreciation allowed or allowable, see chapter 7. For information on adjustments to basis for depreciation allowed or allowable, see chapter 6.

Disposition of plants. If you elect not to use the uniform capitalization rules (see chapter 6), you must treat any plant that would have been subject to the uniform capitalization rules as section 1245 property. If you have a gain on the property's disposition, you must recapture the pre-productive expenses you would have capitalized if you had not made the election by treating the gain, up to the amount of these expenses, as ordinary income. For section 1231 transactions, show these expenses as depreciation on Form 4797, Part III, line 22. For plant sales that are reported on Schedule F (Form 1040), Profit or Loss From Farming, this recapture rule does not change the reporting of income

because the gain is already ordinary income. You can use the farm-price method discussed in chapter 2 to figure these expenses.

Example. You sold your apple orchard in 2024 for \$80,000. Your adjusted basis at the time of sale was \$60,000. You bought the orchard in 2017, but the trees did not produce a crop until 2020. Your pre-productive expenses were \$6,000. You elected not to use the uniform capitalization rules. You must treat \$6,000 of the gain as ordinary income in addition to recapturing depreciation allowed or allowable on the orchard. This amount would be reported on Form 4797, Part III, as ordinary income.



See Uniform Capitalization Rules in chapter 6 for more information regarding electing out of, or being exempt from, using the uniform capitalization rules.

Section 1250 Property

Section 1250 property includes all real property subject to an allowance for depreciation that is not and never has been section 1245 property. It includes buildings and structural components that are not section 1245 property (discussed earlier). It includes a leasehold of land or section 1250 property subject to an allowance for depreciation. A fee simple interest in land is not section 1250 property because, like land, it is not depreciable.

Gain on the disposition of section 1250 property is treated as ordinary income to the extent of additional depreciation allowed or allowable. To determine the additional depreciation on section 1250 property, see *Depreciation Recapture* in chapter 3 of Pub. 544.

Use Part III of Form 4797 to figure the ordinary income part of the gain.

You will not have additional depreciation if any of the following apply to the property disposed of.

- You figured depreciation for the property using the straight line method or any other method that does not result in depreciation that is more than the amount figured by the straight line method and you have held the property longer than 1 year.
- You chose the alternate ACRS (straight line) method for the property, which was a type of 15-, 18-, or 19-year real property covered by the section 1250 rules.
- The property was nonresidential real property placed in service after 1986 (or after July 31, 1986, if the choice to use MACRS was made) and you held it longer than 1 year. These properties are

depreciated using the straight line method.

Installment Sale

If you report the sale of property under the installment method, any depreciation recapture under section 1245 or 1250 is taxable as ordinary income in the year of sale. This applies even if no payments are received in that year. If the gain is more than the depreciation recapture income, report the rest of the gain using the rules of the installment method. For this purpose, include the recapture income in your installment sale basis to determine your gross profit on the installment sale.

If you dispose of more than one asset in a single transaction, you must separately figure the gain on each asset so that it may be properly reported. To do this, allocate the selling price and the payments you receive in the year of sale to each asset. Report any depreciation recapture income in the year of

sale before using the installment method for any remaining gain.

For more information on installment sales, see chapter 10.

Other Dispositions

See chapter 3 of Pub. 544 for the tax treatment of the following transfers of depreciable property.

- By gift.
- At death.
- In like-kind exchanges.
- In involuntary conversions.

Also, see Pub. 544 for information on how to handle a single transaction involving multiple properties.

Other Gains

This section discusses gain on the disposition of farmland for which you were allowed either of the following.

- Deductions for soil and water conservation expenditures (section 1252 property).
- Exclusions from income for certain cost-sharing payments (section 1255 property).

Section 1252 property. If you disposed of farmland you held more than 1 year and less than 10 years at a gain and you were allowed deductions for soil and water conservation expenses for the land, as discussed in chapter 5, you must treat part of the gain as ordinary income and treat the balance as section 1231 gain.

Exceptions. Do not treat gain on the following transactions as gain on section 1252 property.

- Disposition of farmland by gift.
- Transfer of farm property at death (except for income in respect of a decedent).

For more information, see Regulations section 1.1252-2.

Amount to report as ordinary income. You report as ordinary income the lesser of the following amounts.

- Your gain (determined by subtracting the adjusted basis from the amount realized from a sale, exchange, or involuntary conversion, or the fair market value for all other dispositions).
- The total deductions allowed for soil and water conservation expenses multiplied by the applicable percentage, discussed next.

Applicable percentage. The applicable percentage is based on the length of time you held the land. If you dispose of your farmland within 5 years after the date you acquired it,

the percentage is 100%. If you dispose of the land within the sixth through ninth years after you acquired it, the applicable percentage is reduced by 20% a year for each year or part of a year you hold the land after the fifth year. If you dispose of the land 10 or more years after you acquired it, the percentage is 0%, and the entire gain is a section 1231 gain.

Example. You acquired farmland on January 19, 2016. You incurred \$15,000 of soil and water conservation expenditures for the land that were fully deductible. On October 5, 2024, you sold the land at a \$30,000 gain. The applicable percentage is 40% because you sold the land within the eighth year after you acquired it. You treat \$6,000 (40% of \$15,000) of the \$30,000 gain as ordinary income and the \$24,000 balance as a section 1231 gain.

Section 1255 property. If you receive certain cost-sharing payments on property and you exclude those payments from income (as discussed in chapter 3), you may have to treat part of any gain as ordinary income and treat the balance as a section 1231 gain. If you chose not to exclude these payments, you will not have to recognize ordinary income under this provision.

Amount to report as ordinary income. You report as ordinary income the lesser of the following amounts.

- The applicable percentage of the total excluded cost-sharing payments.
- The gain on the disposition of the property.

You do not report ordinary income under this rule to the extent the gain is recognized as ordinary income under sections 1231 through 1254, 1256, and 1257. However, if applicable, gain reported under this rule must

be reported regardless of any contrary provisions (including nonrecognition provisions) under any other section.

Applicable percentage. The applicable percentage of the excluded cost-sharing payments to be reported as ordinary income is based on the length of time you hold the property after receiving the payments. If the property is held less than 10 years after you receive the payments, the percentage is 100%. After 10 years, the percentage is reduced by 10% a year, or part of a year, until the rate is 0%.

Form 4797, Part III. Use Form 4797, Part III, to figure the ordinary income part of a gain from the sale, exchange, or involuntary conversion of section 1252 property and section 1255 property.

10.

Installment Sales

Introduction

An installment sale is a sale of property where you receive at least one payment after the tax year of the sale. If you realize a gain on an installment sale, you may be able to report part of your gain when you receive each payment. This method of reporting gain is called the installment method. You can't use the installment method to report a loss. You can choose to report all of your gain in the year of sale.

Installment obligation. The buyer's obligation to make future payments to you can be in the form of a deed of trust, note, land contract, mortgage, or other evidence of the buyer's debt to you.

Topics

This chapter discusses:

- The general rules that apply to using the installment method, and
- Installment sale of a farm.

Useful Items

You may want to see:

Publication

- ☐ **523** 523 Selling Your Home
- ☐ **537** Installment Sales
- ☐ **538** Accounting Periods and Methods
- ☐ **544** Sales and Other Dispositions of Assets
- ☐ **551** Basis of Assets

Form (and Instructions)

- ☐ **4797** Sales of Business Property
- ☐ **6252** Installment Sale Income

- **8594** Asset Acquisition Statement
Under Section 1060
- **8949** Sales and Other Dispositions of
Capital Assets

See How To Get Tax Help for information about getting publications and forms.

Installment Sale of a Farm

The installment sale of a farm for one overall price under a single contract isn't the sale of a single asset. It generally includes the sale of real property and personal property reportable on the installment method. It may also include the sale of property for which you must maintain an inventory, which can't be reported on the installment method. See Inventory, later. The selling price must be allocated to determine the amount received for each class of asset.

Note. You may be required to report the sale of your farm on Form 8594. For more information, see Form 8594 and its instructions.

The tax treatment of the gain or loss on the sale of each class of asset is determined by its classification as a capital asset, as property used in the business, or as property held for sale and by the length of time the asset was held. (See chapter 8 for a discussion of capital assets and chapter 9 for a discussion of property used in the business.) Separate computations must be made to figure the gain or loss for each class of asset sold. See Sale of a Farm in chapter 8.



If you report the sale of property on the installment method, any depreciation recapture under section 1245 or 1250 is generally taxable as ordinary income in the year of sale. See Depreciation recapture, later. This applies even if no payments are received in that year.

Related parties. If you sell depreciable property to a related person and the sale is an installment sale, you may not be able to report the sale using the installment method. If you sell property to a related person and the related person disposes of the property before you receive all payments with respect to the sale, you may have to treat the amount realized by the related person as received by you when the related person disposes of the property. The definition of related parties differs based on which of these applies. For more information, see *Related Person* under *Sale to a Related Person* in Pub. 537.

Installment Method

An installment sale is a sale of property where you receive at least one payment after the tax year of the sale. A farmer who isn't required to maintain an inventory can use the installment method to report gain from the sale of property used or produced in farming.

See Inventory, later, for information on the sale of farm property where inventory items are included in the assets sold.

If a sale qualifies as an installment sale, the gain must be reported under the installment method unless you elect out of using the installment method.

Electing out of the installment method. If you elect not to use the installment method, you generally report the entire gain in the year of sale, even though you don't receive all the sale proceeds in that year.

To make this election, don't report your sale on Form 6252. Instead, report it on Schedule F (Form 1040), Schedule D (Form 1040), Form 4797, or all three.

You may also need to file Form 8949 along with Schedule D (Form 1040), Capital Gains and Losses. For more information, see Form 8949 and its instructions.

When to elect out. Make this election by the due date, including extensions, for filing your tax return for the year the sale takes place.

However, if you timely file your tax return for the year the sale takes place without making the election, you can still make the election by filing an amended return within 6 months of the due date of the return (excluding extensions). Enter "Filed pursuant to section 301.9100-2" at the top of the amended return. File the amended return at the same address you filed the original return. If you electronically filed your Form 1040 or 1040-SR, you may electronically file the Form 1040-X.

Revoking the election. Once made, the election can be revoked only with IRS approval.

An approved revocation is retroactive.

The taxpayer can't revoke the election if either of the following applies.

- One of the purposes is to avoid federal income tax.
- The tax year in which any payment was received has closed.

To revoke the election, you must obtain a private letter ruling from the IRS. The procedures and user fees for obtaining a private letter ruling are published annually in the first revenue procedure issued each calendar year. For 2024, go to

[IRS.gov/irb/2024-1 IRB#RP-2024-1](https://www.irs.gov/irb/2024-1_IRB#RP-2024-1).

Send your request for a private letter ruling, including the applicable user fee, to the IRS following the instructions in section 7 of Revenue Procedure 2024-1. A schedule of the current user fees is available in Appendix A of Revenue Procedure 2024-1, starting on page 85.

Inventory. If you ***aren't*** required to maintain (keep a record of beginning and ending) inventories under your method of accounting, you can report gain from the sale of farm inventory using the installment method. Complete Form 6252 to figure the amount of installment gain to report each year from the sale of farm inventory and carry that amount to line 8 of Schedule F (Form 1040).

If you ***are*** required to maintain inventories under your method of accounting, you can't report gain from the sale of farm inventory using the installment method. All gain or loss on the sale of farm inventory must be reported in the year of sale, even if you receive payment in later years. If inventory items are included in an installment sale, you may have an agreement stating which payments are for inventory and which are for the other assets being sold. If you don't, each

payment must be allocated between the inventory and the other assets sold.

More information. See *Inventory* under *Sale of a Business* in Pub. 537 for more information.

Sale at a loss. If your sale results in a loss, you can't use the installment method. If the loss is on an installment sale of business assets, you can deduct it only in the tax year of sale.

Figuring Installment Sale Income

Each payment on an installment sale usually consists of the following three parts.

- Interest income.
- Return of your adjusted basis in the property.
- Gain on the sale.

Worksheet 10-1. **Figuring Adjusted Basis and Gross Profit Percentage**

Keep for Your Records



1.	Enter the selling price for the property	_____
2.	Enter your adjusted basis for the property	_____
3.	Enter your selling expenses	_____
4.	Enter any depreciation recapture	_____
5.	Add lines 2, 3, and 4. This is your adjusted basis for installment sale purposes	_____
6.	Subtract line 5 from line 1. If zero or less, enter -0-. This is your gross profit	_____
	If the amount entered on line 6 is zero, stop here. You can't use the installment method.	
7.	Enter the contract price for the property	_____
8.	Divide line 6 by line 7. This is your gross profit percentage	_____

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In each year you receive a payment, you must include in income both the interest part and the part that is your gain on the sale. Don't include in income the part that is the return of your basis in the property. Basis is the amount of your investment in the property for installment sale purposes.

Interest income. You must report interest as ordinary income. Interest generally isn't included in a down payment. However, you may have to treat part of each later payment as interest, even if it isn't called interest in your agreement with the buyer. Interest provided in the agreement is called stated interest. If the agreement doesn't provide for enough stated interest, there may be unstated interest or original issue discount (OID). See *Unstated interest*, later.



You must continue to report the interest income on payments you receive in subsequent years as interest income whether it's stated or unstated.

Adjusted basis and installment sale income (gain on sale). After you have determined how much of each payment to treat as interest, you treat the rest of each payment as if it were made up of two parts.

- A tax-free return of your adjusted basis in the property.
- Your gain (referred to as “installment sale income” on Form 6252).

Figuring adjusted basis and gross profit percentage for installment sale

purposes. You can use Worksheet 10-1 to figure your adjusted basis in the property for installment sale purposes. When you have completed the work-sheet, you will also have determined the gross profit percentage necessary to figure your installment sale income (gain) for this year.

- 1. Selling price.** The selling price is the total cost of the property to the buyer and includes the following.

- Any money you're to receive.
- The fair market value (FMV) of any property you're to receive (FMV is discussed under *Property used as a payment*, later).
- Any existing mortgage or other debt the buyer pays, assumes, or takes the property subject to (a note, a mortgage, or any other liability, such as a lien, accrued interest, or taxes you owe on the property).
- Any of your selling expenses the buyer pays.

Don't include stated interest, unstated interest, any amount recomputed or recharacterized as interest, or OID in the selling price.

2. Adjusted basis. Your adjusted basis in property immediately before the installment sale is your original basis increased or reduced as a result of

various events while you own the property.

- Some events, such as adding rooms or making permanent improvements, increase basis. Others, such as deductible casualty losses or depreciation previously allowed or allowable, decrease basis.
- The way you figure your original basis depends on how you acquire the property. The basis of property you buy is generally its cost. The basis of property you inherit, receive as a gift, build yourself, or receive in a tax-free exchange is figured differently. See chapter 6 and Pub. 551 for more information.
- Generally, your adjusted basis in raised farm products, such as grain or market livestock, is zero.

3. Selling expenses. Selling expenses relate to the sale of the property. Review the closing statement for fees, which may qualify as selling expenses. These may include appraisal fees, attorney fees, closing fees, document preparation fees, escrow fees, mortgage satisfaction fees, notary fees, points paid by the seller to obtain financing for the buyer, real estate broker's commission, recording fees (if paid by the seller), costs of removing title clouds, settlement fees, title search fees, and transfer or stamp taxes charged by city, county, or state governments.

4. Depreciation recapture. If the property you sold was depreciable property:

- You may need to recapture part of the gain on the sale as ordinary income, and See *Depreciation*

*Recapture in chapter 9 and
Depreciation Recapture Income in
Pub. 537.*

5. Adjusted basis for installment sale purposes. Your adjusted basis for installment sale purposes is the total of the following three items.

- Adjusted basis.
- Selling expenses.
- Depreciation recapture.

6. Gross profit. Gross profit is the total gain you report on the installment method.

- To figure your gross profit, subtract your adjusted basis for installment sale purposes from the selling price.
- If the property you sold was your home, subtract from the gross profit any gain you can exclude. See Pub. 523 for more information.

7. Contract price. Contract price equals:

- The selling price, minus
- The amount of any mortgages, debts, and other liabilities assumed or taken by the buyer, plus
- The amount, if any, by which the mortgages, debts, and other liabilities assumed or taken by the buyer exceed your adjusted basis for installment sale purposes.

8. Gross profit percentage. A certain percentage of each payment (after subtracting interest) is reported as installment sale income. This percentage is called the gross profit percentage and is figured by dividing your gross profit from the sale by the contract price.

- The gross profit percentage generally remains the same for each payment you receive. However, see Example

under *Selling price reduced*, later, for a situation where the gross profit percentage changes.

Example. You sell property at a contract price of \$60,000 and your gross profit is \$15,000. Your gross profit percentage is 25% ($\$15,000 \div \$60,000$). After subtracting interest from each payment, you report 25% of each payment, including the down payment, as installment sale income from the sale for the tax year you receive the payment. The remainder (balance) of each payment is the tax-free return of your adjusted basis.

Amount to report as installment sale income. Multiply the payments you receive each year (less interest) by the gross profit percentage. The result is your installment sales income for the tax year. In certain circumstances, you may be treated as having received a payment, even though you received nothing directly. A receipt of

property or the assumption of a mortgage on the property sold may be treated as a payment. For a detailed discussion, see *Payments Received or Considered Received*, later.

Selling price reduced. If the selling price is reduced at a later date, the gross profit on the sale will also change. You must then refigure the gross profit percentage for the remaining payments. Refigure your gross profit using Worksheet 10-2. You will spread any remaining gain over future installments.

Example. In 2022, you sold land with a basis of \$40,000 for \$100,000. Your gross profit was \$60,000. You received a \$20,000 down payment and the buyer's note for \$80,000. The note provides for monthly payments of \$1,953 each, figured at 8% interest, amortized over 4 years, beginning in January 2023. Your gross profit percentage was 60%. You received the down payment of \$20,000 in 2022 and total payments of \$23,436 in 2023,

of which \$17,675 was principal and \$5,761 was interest according to the amortization schedule. You reported a gain of \$12,000 on the down payment received in 2022 and \$10,605 ($\$17,675 \times 60\% (0.60)$) in 2023.

In January 2024, you and the buyer agreed to reduce the purchase price to \$85,000; and payments during 2024, 2025, and 2026 are reduced to \$1,483 a month amortized over the remaining 3 years.

The new gross profit percentage, 47.32%, is figured in Example — Worksheet 10-2.

Worksheet 10-2. **New Gross Profit Percentage — Selling Price Reduced**

Keep for Your Records 

1. Enter the reduced selling price for the property	_____
2. Enter your adjusted basis for the property	_____
3. Enter your selling expenses	_____
4. Enter any depreciation recapture	_____
5. Add lines 2, 3, and 4	_____
6. Subtract line 5 from line 1. This is your adjusted gross profit	_____
7. Enter any installment sale income reported in prior year(s)	_____
8. Subtract line 7 from line 6	_____
9. Future installments	_____
10. Divide line 8 by line 9. This is your new gross profit percentage*	_____

* Apply this percentage to all future payments to determine how much of each of those payments is installment sale income.

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