

# Investment Interest Expense Deduction

▶ Attach to your tax return.

|                         |                    |
|-------------------------|--------------------|
| Name(s) shown on return | Identifying number |
|-------------------------|--------------------|

|   |          |  |
|---|----------|--|
| <b>Part I Total Investment Interest Expense</b>                                   |          |  |
| 1 Investment interest expense paid or accrued in 2002. See instructions . . . . . | 1        |  |
| 2 Disallowed investment interest expense from 2001 Form 4952, line 7 . . . . .    | 2        |  |
| <b>3 Total investment interest expense.</b> Add lines 1 and 2 . . . . .           | <b>3</b> |  |

|  |          |  |
|--|----------|--|
| <b>Part II Net Investment Income</b>   |          |  |
| 4a Gross income from property held for investment (excluding any net gain from the disposition of property held for investment) . . . . .                  | 4a       |  |
| b Net gain from the disposition of property held for investment . . . . .  | 4b       |  |
| c Net capital gain from the disposition of property held for investment . . . . .  | 4c       |  |
| d Subtract line 4c from line 4b. If zero or less, enter -0- . . . . .  | 4d       |  |
| e Enter the amount from line 4c that you elect to include in investment income. Do not enter more than the amount on line 4b. See instructions . . . . . ▶ | 4e       |  |
| f Investment income. Add lines 4a, 4d, and 4e . . . . .  | 4f       |  |
| 5 Investment expenses. See instructions . . . . .  | 5        |  |
| <b>6 Net investment income.</b> Subtract line 5 from line 4f. If zero or less, enter -0- . . . . .   | <b>6</b> |  |

|   |          |  |
|---|----------|--|
| <b>Part III Investment Interest Expense Deduction</b>   |          |  |
| 7 Disallowed investment interest expense to be carried forward to 2003. Subtract line 6 from line 3. If zero or less, enter -0- . . . . . | 7        |  |
| <b>8 Investment interest expense deduction.</b> Enter the <b>smaller</b> of line 3 or 6. See instructions . . . . .                       | <b>8</b> |  |

Section references are to the Internal Revenue Code unless otherwise noted.

## General Instructions

### Purpose of Form

Use Form 4952 to figure the amount of investment interest expense you can deduct for 2002 and the amount you can carry forward to future years. Your investment interest expense deduction is limited to your net investment income.

For more information, see **Pub. 550**, Investment Income and Expenses.

### Who Must File

If you are an individual, estate, or a trust and you claim a deduction for investment interest expense, you must complete Form 4952 and attach it to your tax return.

**Exception.** You do not have to file Form 4952 if **all** of the following apply.

- Your investment interest expense is not more than your investment income from interest and ordinary dividends.
- You have no other deductible investment expenses.
- You have no disallowed investment interest expense from 2001.

## Allocation of Interest Expense Under Temporary Regulations Section 1.163-8T

If you paid or accrued interest on a loan and used the loan proceeds for more than one purpose, you may have to allocate the interest. This is necessary because different rules apply to investment interest, personal interest, trade or business interest, home mortgage interest, and passive activity interest. See **Pub. 535**, Business Expenses.

## Specific Instructions

### Part I—Total Investment Interest Expense

#### Line 1

Enter the investment interest expense paid or accrued during the tax year, regardless of when you incurred the indebtedness. **Investment interest expense** is interest paid or accrued on a loan or part of a loan that is allocable to property held for investment (as defined on page 2).

Include investment interest expense reported to you on Schedule K-1 from a partnership or an S corporation. Include

amortization of bond premium on taxable bonds purchased after October 22, 1986, but before January 1, 1988, unless you elected to offset amortizable bond premium against the interest payments on the bond. A taxable bond is a bond on which the interest is includible in gross income.

Investment interest expense **does not** include any of the following:

- Home mortgage interest.
- Interest expense that is properly allocable to a passive activity. Generally, a passive activity is any business activity in which you **do not** materially participate and any rental activity. See the Instructions for **Form 8582**, Passive Activity Loss Limitations, for details.
- Any interest expense that is capitalized, such as construction interest subject to section 263A.
- Interest expense related to tax-exempt interest income under section 265.
- Interest expense, disallowed under section 264, on indebtedness with respect to life insurance, endowment, or annuity contracts issued after June 8, 1997, even if the proceeds were used to purchase any property held for investment.

**Property held for investment.** Property held for investment includes property that produces income, **not** derived in the ordinary course of a trade or business, from interest, dividends, annuities, or royalties. It also includes property that produces gain or loss, **not** derived in the ordinary course of a trade or business, from the disposition of property that produces these types of income or is held for investment. However, it does not include an interest in a passive activity.

**Exception.** A working interest in an oil or gas property that you held directly or through an entity that did **not** limit your liability is property held for investment, but only if you did not materially participate in the activity.

**Part II—Net Investment Income**

**Line 4a**

Enter your gross income from property held for investment. This includes income, unless derived in the ordinary course of a trade or business, from:

- Interest,
- Ordinary dividends (except Alaska Permanent Fund dividends),
- Annuities, and
- Royalties.

Include investment income reported to you on Schedule K-1 from a partnership or an S corporation. Also include net investment income from an estate or a trust.

Also include on line 4a (or 4b, if applicable) net passive income from a passive activity of a publicly traded partnership (as defined in section 469(k)(2)). See Notice 88-75, 1988-2 C.B. 386, for details.

Net income from certain passive activities, such as rental of substantially nondepreciable property, may have to be recharacterized and included on line 4a. For details, see **Pub. 925**, Passive Activity and At-Risk Rules, or Regulations section 1.469-2(f)(10).

If you are filing **Form 8814**, Parents' Election To Report Child's Interest and Dividends, part or all of your child's income may be included on line 4a. See the instructions for Form 8814 for details.



**Do not include on line 4a any net gain from the disposition of property held for investment. Instead, enter it on line 4b.**

**Line 4b**

Enter your net gain from the disposition of property held for investment. This is the excess, if any, of your total gains over your total losses from the disposition of property held for investment. When figuring this amount, include capital gain distributions from mutual funds.

**Line 4c**

Enter your net capital gain from the disposition of property held for investment. This is the excess, if any, of your net long-term capital gain over your net short-term capital loss from the disposition of property held for investment.

Capital gain distributions from mutual funds are treated as long-term capital gains.

**Line 4e**

Net capital gain from the disposition of property held for investment, line 4c, is excluded from investment income. However, you may elect to include in investment income part or all of the net capital gain from the disposition of property held for investment. If you make this election, you must reduce the amount of net capital gain eligible for capital gains tax rates by the amount of net capital gain you include in investment income. Therefore, you should consider the tax effect of using the capital gains tax rates before making this election. Once made, the election may only be revoked with IRS consent.

To make the election, enter on line 4e the amount you elect to include in investment income. Also enter this amount on line 22 of Schedule D (Form 1040), or on line 20 of Schedule D (Form 1041), if applicable.

You must generally make this election on a timely filed return, including extensions. However, if you timely filed your return without making the election, you can make the election on an amended return filed within 6 months of the due date of your return (excluding extensions). Write "Filed pursuant to section 301.9100-2" on the amended return and file it at the same place you filed the original return.

**Line 5**

Investment expenses are your allowed deductions, other than interest expense, directly connected with the production of investment income. For example, depreciation or depletion allowed on assets that produce investment income is an investment expense.

Include investment expenses reported to you on Schedule K-1 from a partnership or an S corporation.

Investment expenses **do not** include any deductions used in determining your income or loss from a passive activity.

If you have investment expenses that are included as a miscellaneous itemized deduction on Schedule A (Form 1040), line 22, the 2% adjusted gross income limitation on Schedule A (Form 1040), line 25, may reduce the amount you must include on Form 4952, line 5. Include on line 5 the **smaller** of:

- The investment expenses included on Schedule A (Form 1040), line 22, or
- The total on Schedule A (Form 1040), line 26.

**Part III—Investment Interest Expense Deduction**

**Line 8**

You may deduct the amount on line 8 as investment interest expense.

**Individuals.** Generally, enter the amount from line 8 on Schedule A (Form 1040), line 13, even if all or part of it is attributable to a partnership or an S corporation. However, if any part of the interest expense is attributable to royalties, enter that part on Schedule E (Form 1040). Also, if any part of the interest is attributable to a trade or business that is not a passive activity, enter that part on the schedule where you report other expenses for that trade or business.

**Estates and trusts.** Enter the amount from line 8 on Form 1041, line 10.

**Form 6198.** If any of your deductible investment interest expense is attributable to an activity for which you are not at risk, you must also use **Form 6198**, At-Risk Limitations, to figure your deductible investment interest expense. Enter the part attributable to the at-risk activity on Form 6198, line 4. Reduce Form 4952, line 8, by the amount entered on Form 6198.

**Alternative minimum tax (AMT).** Deductible interest expense may be an adjustment for the AMT. For details, see **Form 6251**, Alternative Minimum Tax—Individuals, or Form 1041, Schedule I, for estates and trusts.

**Paperwork Reduction Act Notice.** We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

|   |         |
|---|---------|
| <b>Recordkeeping</b> . . . . .  | 13 min. |
| <b>Learning about the law or the form</b> . . . . .                   | 16 min. |
| <b>Preparing the form</b> . . . . .                                   | 21 min. |
| <b>Copying, assembling, and sending the form to the IRS</b> . . . . . | 10 min. |

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. See the instructions for the tax return with which this form is filed.

