Form **4952**

Department of the Treasury
Internal Revenue Service (99)

Investment Interest Expense Deduction

▶ **Attach to your tax return.**

OMB No. 1545-0191

2007

Attachment Sequence No. **51**

Name(s) shown on return

Identifying number

Draft as of 04/10/2007

Part I **Total Investment Interest Expense**

1	Investment interest expense paid or accrued in 2007 (see instructions)	1	
2	Disallowed investment interest expense from 2006 Form 4952, line 7	2	
3	**Total investment interest expense.** Add lines 1 and 2	3	

Part II **Net Investment Income**

4a	Gross income from property held for investment (excluding any net gain from the disposition of property held for investment)	4a		
b	Qualified dividends included on line 4a	4b		
c	Subtract line 4b from line 4a		4c	
d	Net gain from the disposition of property held for investment	4d		
e	Enter the **smaller** of line 4d or your net capital gain from the disposition of property held for investment (see instructions)	4e		
f	Subtract line 4e from line 4d		4f	
g	Enter the amount from lines 4b and 4e that you elect to include in investment income (see instructions)		4g	
h	Investment income. Add lines 4c, 4f, and 4g		4h	
5	Investment expenses (see instructions)		5	
6	**Net investment income.** Subtract line 5 from line 4h. If zero or less, enter -0-		6	

Part III **Investment Interest Expense Deduction**

7	Disallowed investment interest expense to be carried forward to 2008. Subtract line 6 from line 3. If zero or less, enter -0-	7	
8	**Investment interest expense deduction.** Enter the **smaller** of line 3 or 6. See instructions	8	

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 2007 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, you must file Form 4952 to claim a deduction for your investment interest expense.

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

- Your investment income from interest and ordinary dividends minus any qualified dividends is more than your investment interest expense.
- You do not have any other deductible investment expenses.
- You do not have any carryover of disallowed investment interest expense from 2006.

Allocation of Interest Expense

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 this page).

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 trade or 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

Gross income from property held for investment 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 4d, 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.

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

Line 4b

Enter the portion of ordinary dividends included on line 4a that are qualified dividends. For the definition of qualified dividends, see the instructions for Form 1040, line 9b (or Form 1041, line 2b).

Line 4d

Net gain from the disposition of property held for investment 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 and capital loss carryovers.

Line 4e

Net capital gain from the disposition of property held for investment 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.

Note. If line 4e is more than zero and you enter an amount on line 4g, see the *Note* in the line 4g instructions.

Line 4g

In general, qualified dividends and net capital gain from the disposition of property held for investment are excluded from investment income. But you can elect to include part or all of these amounts in investment income.

CAUTION *The qualified dividends and net capital gain that you elect to include in investment income on line 4g are not eligible to be taxed at the qualified dividends or capital gains tax rates. You should consider the tax effect of using the qualified dividends and capital gains tax rates before making this election. Once made, the election can be revoked only with IRS consent.*

To make the election, enter on line 4g the amount you elect to include in investment income (do not enter more than the sum of lines 4b and 4e). Also enter this amount on whichever of the following applies.

- The Qualified Dividends and Capital Gain Tax Worksheet, line 5, in the Instructions for Form 1040.
- The Schedule D Tax Worksheet, line 3.
- Schedule D (Form 1041), line 21.
- The Qualified Dividends Tax Worksheet, line 3, in the Instructions for Form 1041.

Do not reduce the amount of qualified dividends on Form 1040, line 9b (or Form 1041, line 2b(2)), by any part of the amount on line 4g.

Note. The amount on line 4g is generally treated as being attributable first to net capital gain from property held for investment (line 4e), and then to qualified dividends (line 4b). This treatment results in the least tax being figured for Form 1040, line 44 (or Form 1041, Schedule G, line 1a). However, you can treat less of the amount on line 4e as attributable to line 4g and more to line 4b. You may want to do this if you are filing Form 1116, Foreign Tax Credit, as your tax after credits may be lower in certain cases. To do so, enter on the dotted line next to line 4e "Elec." and the part of line 4e that you elect to treat as being attributable to line 4g (do not enter less than the excess of line 4g over line 4b). You will use this smaller amount instead of the amount on line 4e when figuring your tax.

Generally, you must 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 23, the 2% adjusted gross income limitation on Schedule A (Form 1040), line 26, may reduce the amount you must include on Form 4952, line 5. Include on line 5 the smaller of: (a) the investment expenses included on Schedule A (Form 1040), line 23, or (b) the total on Schedule A (Form 1040), line 27.

Part III—Investment Interest Expense Deduction

Line 8

Individuals. Generally, enter the amount from line 8 (excluding any amount included on Form 6198, line 4—see below) on Schedule A (Form 1040), line 14, 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 (excluding any amount included on Form 6198, line 4—see below) 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. Include the part attributable to the at-risk activity on Form 6198, line 4.

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).

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 burden for individual taxpayers filing this form is approved under OMB control number 1545-0074 and is included in the estimates shown in the instructions for their individual income tax return. The estimated burden for all other taxpayers who file this form is shown below. **Recordkeeping,** 39 min.; **Learning about the law or the form,** 12 min.; **Preparing the form,** 22 min.; and **Copying, assembling, and sending the form to the IRS,** 13 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.

Draft as of 08/10/2007