

Publication 525

Taxable and Nontaxable Income

For use in preparing

2024 Returns

Volume 3 of 5



Get forms and other information faster and easier at:

- [IRS.gov](https://www.irs.gov) (English)
- [IRS.gov/Korean](https://www.irs.gov/korean) (한국어)
- [IRS.gov/Spanish](https://www.irs.gov/spanish) (Español)
- [IRS.gov/Russian](https://www.irs.gov/russian) (Русский)
- [IRS.gov/Chinese](https://www.irs.gov/chinese) (中文)
- [IRS.gov/Vietnamese](https://www.irs.gov/vietnamese) (Tiếng Việt)



Publication 525 (Rev 2024) Catalog Number 39277Z
Department of the Treasury **Internal Revenue Service** www.irs.gov



Visit the Accessibility
Page on [IRS.gov](https://www.irs.gov)

This page is intentionally left blank

Partnership Income

A partnership generally isn't a taxable entity. The income, gains, losses, deductions, and credits of a partnership are passed through to the partners based on each partner's distributive share of these items. For more information, see Pub. 541.

Partner's distributive share. Your distributive share of partnership income, gains, losses, deductions, or credits is generally based on the partnership agreement. You must report your distributive share of these items on your return whether or not they are actually distributed to you. However, your distributive share of the partnership losses is limited to the adjusted basis of your partnership interest at the end of the partnership year in which the losses took place.

Partnership agreement. The partnership agreement usually covers the distribution of profits, losses, and other items.

However, if the agreement doesn't state how a specific item of gain or loss will be shared, or the allocation stated in the agreement doesn't have substantial economic effect, your distributive share is figured according to your interest in the partnership.

Partnership return. Although a partnership generally pays no tax, it must file an information return on Form 1065. This shows the result of the partnership's operations for its tax year and the items that must be passed through to the partners.

Schedule K-1 (Form 1065). You should receive from each partnership in which you're a member a copy of Schedule K-1 (Form 1065) showing your share of income, deductions, credits, and tax preference items of the partnership for the tax year. Keep Schedule K-1 for your records. Don't attach it to your Form 1040 or 1040-SR, unless you're specifically required to do so.

Partner's return. You must generally report partnership items on your individual return the same way as they're reported on the partnership return. That is, if the partnership had a capital gain, you report your share as explained in the Instructions for Schedule D (Form 1040). You report your share of partnership ordinary income on Schedule E (Form 1040).



In many cases, Schedule K-1 (Form 1065) will tell you where to report an item of income on your individual return.

Qualified joint venture. If you and your spouse each materially participate as the only members of a jointly owned and operated business, and you file a joint return for the tax year, you can make a joint election to be treated as a qualified joint venture instead of a partnership.

To make this election, you must divide all items of income, gain, loss, deduction, and credit attributable to the business between you and your spouse in accordance with your respective interests in the venture. For further information on how to make the election and which schedule(s) to file, see the instructions for your individual tax return.

S Corporation Income

In most cases, an S corporation doesn't pay tax on its income. Instead, the income, losses, deductions, and credits of the corporation are passed through to the shareholders based on each shareholder's pro rata share. You must report your share of these items on your return. In most cases, the items passed through to you will increase or decrease the basis of your S corporation stock as appropriate.

S corporation return. An S corporation must file a return on Form 1120-S. This shows the results of the corporation's operations for its tax year and the items of income, losses, deductions, or credits that affect the shareholders' individual income tax returns.

Schedule K-1 (Form 1120-S). You should receive a copy of Schedule K-1 (Form 1120-S) from any S corporation in which you're a shareholder. Schedule K-1 (Form 1120-S) shows your share of income, losses, deductions, and credits for the tax year. Keep Schedule K-1 (Form 1120-S) for your records. Don't attach it to your Form 1040 or 1040-SR, unless you're specifically required to do so.

Shareholder's return. Your distributive share of the items of income, losses, deductions, or credits of the S corporation must be shown separately on your Form 1040 or 1040-SR.

The character of these items is generally the same as if you had realized or incurred them personally.



In many cases, Schedule K-1 (Form 1120-S) will tell you where to report an item of income on your individual return.

Distributions. In most cases, S corporation distributions are a nontaxable return of your basis in the corporation stock. However, in certain cases, part of the distributions may be taxable as a dividend, or as a long-term or short-term capital gain, or as both. The corporation's distributions may be in the form of cash or property.

More information. For more information, see the Instructions for Form 1120-S.

Sickness and Injury Benefits

In most cases, you must report as income any amount you receive for personal injury or sickness through an accident or health plan that is paid for by your employer. If both you and your employer pay for the plan, only the amount you receive that is due to your employer's payments is reported as income. However, certain payments may not be taxable to you. For information on nontaxable payments, see *Military and Government Disability Pensions* and *Other Sickness and Injury Benefits*, later in this discussion.



Don't report as income any amounts paid to reimburse you for medical expenses you incurred after the plan was established.

Cost paid by you. If you pay the entire cost of an accident or health plan, don't include any amounts you receive from the plan for personal injury or sickness as income on your

tax return. If your plan reimbursed you for medical expenses you deducted in an earlier year, you may have to include some, or all, of the reimbursement in your income.

See Recoveries under *Miscellaneous Income*, later.

Cafeteria plans. In most cases, if you're covered by an accident or health insurance plan through a cafeteria plan, and the amount of the insurance premiums wasn't included in your income, you aren't considered to have paid the premiums and you must include any benefits you receive in your income. If the amount of the premiums was included in your income, you're considered to have paid the premiums and any benefits you receive aren't taxable.

Disability Pensions

If you retired on disability, you must include in income any disability pension you receive under a plan that is paid for by your employer.

You must report your taxable disability payments on line 1h of Form 1040 or 1040-SR until you reach minimum retirement age. Minimum retirement age is generally the age at which you can first receive a pension or annuity if you aren't disabled.



You may be entitled to a tax credit if you were permanently and totally disabled when you retired. For information on this credit, see Pub. 524.

Beginning on the day after you reach minimum retirement age, payments you receive are taxable as a pension or annuity. Report the payments on lines 5a and 5b of Form 1040 or 1040-SR. For more information on pensions and annuities, see Pub. 575.

Terrorist attacks or military action. Don't include in your income disability payments you receive for injuries incurred as a direct result of terrorist attacks or military action directed against the United States

(or its allies), whether outside or within the United States. In the case of the September 11 attacks, injuries eligible for coverage by the September 11 Victim Compensation Fund are treated as incurred as a direct result of the attack. However, you must include in your income any amounts that you received that you would have received in retirement had you not become disabled as a result of a terrorist attack or military action. Accordingly, you must include in your income any payments you receive from a 401(k), pension, or other retirement plan to the extent that you would have received the amount at the same or later time regardless of whether you had become disabled. See Pub. 907.

A terrorist action is one that is directed against the United States or any of its allies (including a multinational force in which the United States is participating).

A military action is one that involves the U.S. Armed Forces and is a result of actual or threatened violence or aggression against the United States or any of its allies, but doesn't include training exercises.



Contact the company or agency making these payments if it incorrectly reports your payments as taxable income to the IRS on Form W-2, or on Form 1099-R, to request that it reissue the form to report some or all of these payments as nontaxable income in box 12 (under code J) of Form W-2 or in box 1 but not in box 2a of Form 1099-R. If income taxes are being incorrectly withheld from these payments, you may also submit Form W-4 to the company or agency to stop the withholding of income taxes from payments reported on Form W-2 or you may submit Form W-4P to stop the withholding of income taxes from payments reported on Form 1099-R.

Disability payments you receive for injuries not incurred as a direct result of a terrorist attack or military action or for illnesses or diseases not resulting from an injury incurred as a direct result of a terrorist attack or military action can't be excluded from your income under this provision but may be excludable for other reasons. See Pub. 907.

Retirement and profit-sharing plans. If you receive payments from a retirement or profit-sharing plan that doesn't provide for disability retirement, don't treat the payments as a disability pension. The payments must be reported as a pension or annuity.

Accrued leave payment. If you retire on disability, any lump-sum payment you receive for accrued annual leave is a salary payment. The payment isn't a disability payment. Include it in your income in the tax year you receive it.

Military and Government Disability Pensions

Certain military and government disability pensions aren't taxable.

Service-connected disability. You may be able to exclude from income amounts you receive as a pension, annuity, or similar allowance for personal injury or sickness resulting from active service in one of the following government services.

- The armed forces of any country.
- The National Oceanic and Atmospheric Administration.
- The Public Health Service.
- The Foreign Service.

Conditions for exclusion. Don't include the disability payments in your income if any of the following conditions apply.

1. You were entitled to receive a disability payment before September 25, 1975.
2. You were a member of a listed government service or its reserve component, or were under a binding written commitment to become a member, on September 24, 1975.
3. You receive the disability payments for a combat-related injury. This is a personal injury or sickness that:
 - a. Results directly from armed conflict;
 - b. Takes place while you're engaged in extra-hazardous service;
 - c. Takes place under conditions simulating war, including training exercises such as maneuvers; or

- d. Is caused by an instrumentality of war.
- 4. You would be entitled to receive disability compensation from the VA if you filed an application for it. Your exclusion under this condition is equal to the amount you would be entitled to receive from the VA.

Pension based on years of service. If you receive a disability pension based on years of service, in most cases, you must include it in your income. However, if the pension qualifies for the exclusion for a service-connected disability (discussed earlier), don't include in income the part of your pension that you would have received if the pension had been based on a percentage of disability. You must include the rest of your pension in your income.

Retroactive VA determination. If you retire from the U.S. Armed Forces based on years of service and are later given a retroactive service-connected disability rating by the VA, your retirement pay for the retroactive period is excluded from income up to the amount of VA disability benefits you would have been entitled to receive. You can claim a refund of any tax paid on the excludable amount (subject to the statute of limitations) by filing an amended return on Form 1040-X for each previous year during the retroactive period. You must include with each Form 1040-X a copy of the official VA determination letter granting the retroactive benefit. The letter must show the amount withheld and the effective date of the benefit.

Generally, the VA determination letter will contain a table with five headings. The table on the letter must cover the same dates for the tax year reported on the Form 1040-X.

To calculate the correct tax reduction, multiply the Effective Months by the Amount Withheld for the tax year. For example, Form 1040-X was filed for tax year 2021. The table shows the Amount Withheld effective December 2020 is \$320.00. To calculate the amount for the tax reduction, multiply the 2021 Effective Months by the Amount Withheld. In this case, January–December (2021) is 12 months x \$320.00 (Amount Withheld) = \$3,840.00; this amount should be the amount claimed as a reduction on Line 1 Adjusted Gross Income (AGI), Column B, of the 2021 Form 1040-X.

If you receive a lump-sum disability severance payment and are later awarded VA disability benefits, exclude 100% of the severance benefit from your income. However, you must include in your income any lump-sum readjustment or other

nondisability severance payment you received on release from active duty, even if you're later given a retroactive disability rating by the VA.

Special statute of limitations. In most cases, under the statute of limitations a claim for credit or refund must be filed within 3 years from the time a return was filed.

However, if you receive a retroactive service-connected disability rating determination, the statute of limitations is extended by a 1-year period beginning on the date of the determination. This 1-year extended period applies to claims for credit or refund filed after June 17, 2008, and doesn't apply to any tax year that began more than 5 years before the date of the determination.

Example 19. You retired in 2018 and receive a pension based on your years of service. On August 3, 2024, you receive a determination of service-connected disability retroactive to 2018.

Generally, you could claim a refund for the taxes paid on your pension for 2021, 2022, and 2023. However, under the special limitation period, you can also file a claim for 2020 as long as you file the claim by August 3, 2025. You can't file a claim for 2018 and 2019 because those tax years began more than 5 years before the determination.

Combat-related special compensation.

Combat-related special compensation, as described under 10 U.S.C. section 1413a, is a specific entitlement only payable to retirees of the Uniformed Services. If you're in receipt of combat-related special compensation, you may exclude the amount of your combat-related special compensation from your income. Other portions of your military or disability retirement pay may still be included in your income.

Terrorist attack or military action. Don't include in your income disability payments you receive for injuries resulting directly from

a terrorist or military action. In the case of the September 11 attacks, injuries eligible for coverage by the September 11 Victim Compensation Fund are treated as incurred as a direct result of the attack. However, you must include in your income any amounts that you received that you would have received in retirement had you not become disabled as a result of a terrorist or military action. Accordingly, you must include in your income any payments you receive from a 401(k), pension, or other retirement plan to the extent that you would have received the amount at the same or later time regardless of whether you had become disabled.

Disability payments you receive for injuries not incurred as a direct result of a terrorist or military action or for illnesses or diseases not resulting from an injury incurred as a direct result of a terrorist or military action may be excludable from income for other reasons.

See Pub. 907.

A terrorist action is one that is directed against the United States or any of its allies (including a multinational force in which the United States is participating). A military action is one that involves the U.S. Armed Forces and is a result of actual or threatened violence or aggression against the United States or any of its allies, but doesn't include training exercises.

Long-Term Care Insurance Contracts

In most cases, long-term care insurance contracts are treated as accident and health insurance contracts. Amounts you receive from them (other than policyholder dividends or premium refunds) are excludable in most cases from income as amounts received for personal injury or sickness. To claim an exclusion for payments made on a per diem or other periodic basis under a long-term care insurance contract, you must file Form 8853 with your return.

A long-term care insurance contract is an insurance contract that only provides coverage for qualified long-term care services. The contract must:

- Be guaranteed renewable;
- Not provide for a cash surrender value or other money that can be paid, assigned, pledged, or borrowed;
- Provide that refunds, other than refunds on the death of the insured or complete surrender or cancellation of the contract, and dividends under the contract may be used only to reduce future premiums or increase future benefits; and
- In most cases, not pay or reimburse expenses incurred for services or items that would be reimbursed under Medicare, except where Medicare is a secondary payer or the contract makes per diem or other periodic payments without regard to expenses.

Qualified long-term care services.

Qualified long-term care services are:

- Necessary diagnostic, preventive, therapeutic, curing, treating, mitigating, rehabilitative services, and maintenance and personal care services; and
- Required by a chronically ill individual and provided pursuant to a plan of care prescribed by a licensed health care practitioner.

Chronically ill individual. A chronically ill individual is one who has been certified by a licensed health care practitioner within the previous 12 months as one of the following.

- An individual who, for at least 90 days, is unable to perform at least two activities of daily living without substantial assistance due to a loss of functional capacity. Activities of daily living are eating, toileting, transferring, bathing, dressing, and continence.

- An individual who requires substantial supervision to be protected from threats to health and safety due to severe cognitive impairment.

Limit on exclusion. The exclusion for payments made on a per diem or other periodic basis under a long-term care insurance contract is subject to a limit. The limit applies to the total of these payments and any accelerated death benefits made on a per diem or other periodic basis under a life insurance contract because the insured is chronically ill. (For more information on accelerated death benefits, see *Life Insurance Proceeds* under *Miscellaneous Income*, later.)

Under this limit, the excludable amount for any period is figured by subtracting any reimbursement received (through insurance or otherwise) for the cost of qualified long-term care services during the period from the larger of the following amounts.

- The cost of qualified long-term care services during the period.
- The dollar amount for the period (\$410 per day for any period in 2024).

See Section C of Form 8853 and its instructions for more information.

Workers' Compensation

Amounts you receive as workers' compensation for an occupational sickness or injury are fully exempt from tax if they're paid under a workers' compensation act or a statute in the nature of a workers' compensation act. The exemption also applies to your survivors. The exemption, however, doesn't apply to retirement plan benefits you receive based on your age, length of service, or prior contributions to the plan, even if you retired because of an occupational sickness or injury.



If part of your workers' compensation reduces your social security or equivalent railroad retirement benefits received, that part is considered social security (or equivalent railroad retirement) benefits and may be taxable. See Pub. 554 and Pub. 915, Social Security and Equivalent Railroad Retirement Benefits, for more information.

Return to work. If you return to work after qualifying for workers' compensation, salary payments you receive for performing light duties are taxable as wages.

Disability pension. If your disability pension is paid under a statute that provides benefits only to employees with service-connected disabilities, part of it may be workers' compensation. That part is exempt from tax. The rest of your pension, based on years of service, is taxable as pension or annuity income.

If you die, the part of your survivors' benefit that is a continuation of the workers' compensation is exempt from tax.

Other Sickness and Injury Benefits

In addition to disability pensions and annuities, you may receive other payments for sickness or injury.

Railroad sick pay. Payments you receive as sick pay under the Railroad Unemployment Insurance Act are taxable and you must include them in your income. However, don't include them in your income if they're for an on-the-job injury.

Black lung benefit payments. These payments are similar to workers' compensation and aren't taxable in most cases.

Federal Employees' Compensation Act (FECA). Payments received under FECA for personal injury or sickness, including payments to beneficiaries in case of death,

aren't taxable. However, you're taxed on amounts you receive under FECA as continuation of pay for up to 45 days while a claim is being decided. Report this income on line 1a of Form 1040 or 1040-SR. Also, pay for sick leave while a claim is being processed is taxable and must be included in your income as wages.



If part of the payments you receive under FECA reduces your social security or equivalent railroad retirement benefits received, that part is considered social security (or equivalent railroad retirement) benefits and may be taxable. See Pub. 554 for more information.

Qualified Indian health care benefit. For benefits and coverage provided after March 23, 2010, the value of any qualified Indian health care benefit isn't taxable.

These benefits include any health service or benefits provided by the Indian Health Service, amounts to reimburse medical care expenses provided by an Indian tribe, coverage under accident or health insurance, and any other medical care provided by an Indian tribe.

Other compensation. Many other amounts you receive as compensation for sickness or injury aren't taxable. These include the following amounts.

- Compensatory damages you receive for physical injury or physical sickness, whether paid in a lump sum or in periodic payments. See Court awards and damages under *Other Income*, later.
- Benefits you receive under an accident or health insurance policy on which either you paid the premiums or your employer paid the premiums but you had to include them in your income.

- Disability benefits you receive for loss of income or earning capacity as a result of injuries under a no-fault car insurance policy.
- Compensation you receive for permanent loss or loss of use of a part or function of your body, or for your permanent disfigurement. This compensation must be based only on the injury and not on the period of your absence from work. These benefits aren't taxable even if your employer pays for the accident and health plan that provides these benefits.

Reimbursement for medical care. A reimbursement for medical care is generally not taxable. However, it may reduce your medical expense deduction. If you receive reimbursement for an expense you deducted in an earlier year, see Recoveries, later.

If you receive an advance reimbursement or loan for future medical expenses from your employer without regard to whether you suffered a personal injury or sickness or incurred medical expenses, that amount is included in your income, whether or not you incur uninsured medical expenses during the year.

Reimbursements received under your employer's plan for expenses incurred before the plan was established are included in income.

Amounts you receive under a reimbursement plan that provides for the payment of unused reimbursement amounts in cash or other benefits are included in your income. For details, see Pub. 969.

Miscellaneous Income

This section discusses various types of income. You may have taxable income from certain transactions even if no money

changes hands. For example, you may have taxable income if you lend money at a below-market interest rate or have a debt you owe canceled.

Bartering

Bartering is an exchange of property or services. You must include in your income, at the time received, the FMV of property or services you receive in bartering. If you exchange services with another person and you both have agreed ahead of time on the value of the services, that value will be accepted as FMV unless the value can be shown to be otherwise.

Generally, you report this income on Schedule C (Form 1040). However, if the barter involves an exchange of something other than services, such as in Example 23, later, you may have to use another form or schedule instead.

Example 20. You're a self-employed attorney who performs legal services for a client, a small corporation. The corporation gives you shares of its stock as payment for your services. You must include the FMV of the shares in your income on Schedule C (Form 1040) in the year you receive them.

Example 21. You're a self-employed accountant. You and a house painter are members of a barter club. Members contact each other directly and bargain for the value of the services to be performed. In return for accounting services you provided, the house painter painted your home. You must report as your income on Schedule C (Form 1040) the FMV of the house painting services you received. The house painter must include in income the FMV of the accounting services you provided.

Example 22. You're self-employed and a member of a barter club. The club uses credit units as a means of exchange.

It adds credit units to your account for goods or services you provide to members, which you can use to purchase goods or services offered by other members of the barter club. The club subtracts credit units from your account when you receive goods or services from other members. You must include in your income the value of the credit units that are added to your account, even though you may not actually receive goods or services from other members until a later tax year.

Example 23. You own a small apartment building. In return for 6 months rent-free use of an apartment, an artist gives you a work of art she created. You must report as rental income on Schedule E (Form 1040) the FMV of the artwork, and the artist must report as income on Schedule C (Form 1040) the fair rental value of the apartment.

Form 1099-B from barter exchange. If you exchanged property or services through a barter exchange,

Form 1099-B or a similar statement from the barter exchange should be sent to you by February 15, 2025. It should show the value of cash, property, services, credits, or scrip you received from exchanges during 2024. The IRS will also receive a copy of Form 1099-B.

Backup withholding. In most cases, the income you receive from bartering isn't subject to regular income tax withholding. However, backup withholding will apply in certain circumstances to ensure that income tax is collected on this income.

Under backup withholding, the barter exchange must withhold, as income tax, 24% of the income if:

- You don't give the barter exchange your TIN, or
- The IRS notifies the barter exchange that you gave it an incorrect TIN.

If you join a barter exchange, you must certify under penalties of perjury that your TIN is correct and that you aren't subject to backup withholding. If you don't make this certification, backup withholding may begin immediately. The barter exchange will give you a Form W-9, or a similar form, for you to make this certification. The barter exchange will withhold tax only up to the amount of any cash paid to you or deposited in your account and any scrip or credit issued to you (and converted to cash).



If tax is withheld from your barter income, the barter exchange will report the amount of tax withheld on Form 1099-B or similar statement.

Canceled Debts

In most cases, if a debt you owe is canceled or forgiven, other than as a gift or bequest, you must include the canceled amount in your income.

You have no income from the canceled debt if it's intended as a gift to you. A debt includes any indebtedness for which you're liable or which attaches to property you hold.

If the debt is a nonbusiness debt, report the canceled amount on Schedule 1 (Form 1040), line 8c. If it's a business debt, report the amount on Schedule C (Form 1040) or on Schedule F (Form 1040) if the debt is farm debt and you're a farmer.

Starting in 2014, you must include the income you elected to defer in 2009 or 2010 from a cancellation, reacquisition, or modification of a business debt. For information on this election, see Revenue Procedure 2009-37, available at [IRS.gov/irb/2009-36_IRB#RP-2009-37](https://www.irs.gov/irb/2009-36_IRB#RP-2009-37).

Form 1099-C. If a federal government agency, financial institution, or credit union cancels or forgives a debt you owe of \$600 or more, you may receive a Form 1099-C.

Form 1099-C, box 2, shows the amount of debt either actually or deemed discharged. If you don't agree with the amount reported in box 2, contact your creditor.

Interest included in canceled debt. If any interest is forgiven and included in the amount of canceled debt in box 2, the amount of interest will also be shown in box 3. Whether or not you must include the interest portion of the canceled debt in your income depends on whether the interest would be deductible if you paid it. See *Deductible debt* under *Exceptions*, later.

If the interest would not be deductible (such as interest on a personal loan), include in your income the amount from box 2 of Form 1099-C. If the interest would be deductible (such as on a business loan), include in your income the net amount of the canceled debt (the amount shown in box 2 less the interest amount shown in box 3).

Discounted mortgage loan. If your financial institution offers a discount for the early payment of your mortgage loan, the amount of the discount is canceled debt. You must include the canceled amount in your income.

Mortgage relief upon sale or other disposition. If you're personally liable for a mortgage (recourse debt), and you're relieved of the mortgage when you dispose of the property, you may realize gain or loss up to the FMV of the property. To the extent the mortgage discharge exceeds the FMV of the property, it's income from discharge of indebtedness unless it qualifies for exclusion under Excluded debt, later. Report any income from discharge of indebtedness on nonbusiness debt that doesn't qualify for exclusion as other income on Schedule 1 (Form 1040), line 8c.



You may be able to exclude part of the mortgage relief on your principal residence. See Excluded debt, later.

If you aren't personally liable for a mortgage (nonrecourse debt), and you're relieved of the mortgage when you dispose of the property

(such as through foreclosure), that relief is included in the amount you realize.

You may have a taxable gain if the amount you realize exceeds your adjusted basis in the property. Report any gain on nonbusiness property as a capital gain. See Pub. 4681 for more information.

Stockholder debt. If you're a stockholder in a corporation and the corporation cancels or forgives your debt to it, the canceled debt is a constructive distribution that is generally dividend income to you. For more information, see Pub. 542.

If you're a stockholder in a corporation and you cancel a debt owed to you by the corporation, you generally don't realize income. This is because the canceled debt is considered as a contribution to the capital of the corporation equal to the amount of debt principal that you canceled.

Repayment of canceled debt. If you included a canceled amount in your income and later pay the debt, you may be able to file a claim for refund for the year the amount was included in income. You can file a claim on Form 1040-X if the statute of limitations for filing a claim is still open. The statute of limitations generally doesn't end until 3 years after the due date of your original return.

Exceptions

There are several exceptions to the inclusion of canceled debt in income. These are explained next.

Student loans. Generally, if you're responsible for making loan payments, and the loan is canceled or repaid by someone else, you must include the amount that was canceled or paid on your behalf in your gross income for tax purposes. However, in certain circumstances, you may be able to exclude amounts from gross income as a result of the cancellation or repayment of certain student loans. These exclusions are for:

- Student loan cancellation due to meeting certain work requirements;
- Cancellation of certain loans after December 31, 2020, and before January 1, 2026 (see *Special rule for student loan discharges for 2021 through 2025*); or
- Certain student loan repayment assistance programs.

Exclusion for student loan cancellation due to meeting certain work requirements.

If your student loan is canceled in part or in whole in 2024 due to meeting certain work requirements, you may not have to include the canceled debt in your income. To qualify for this work-related exclusion, your loan must have been made by a qualified lender to assist you in attending an eligible educational organization described in section 170(b)(1)(A)(ii). In addition, the cancellation must be pursuant to a provision in the student loan that all or part of the debt will be canceled if you work:

- For a certain period of time,
- In certain professions, and
- For any of a broad class of employers.



The cancellation of your loan won't qualify for tax-free treatment if it was made by an educational organization or tax-exempt section 501(c)(3) organization

and was canceled because of the services you performed for either organization. See Exception, later.

Educational organization described in section 170(b)(1)(A)(ii). This is an educational organization that maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where it carries on its educational activities.

Qualified lenders. These include the following.

1. The United States, or an instrumentality or agency thereof.
2. A state or territory of the United States; or the District of Columbia; or any political subdivision thereof.
3. A public benefit corporation that is tax-exempt under section 501(c)(3); and that has assumed control of a state, county, or municipal hospital; and

whose employees are considered public employees under state law.

4. An educational organization described in section 170(b)(1)(A)(ii), if the loan is made:
 - a. As part of an agreement with an entity described in (1), (2), or (3) under which the funds to make the loan were provided to the educational organization; or
 - b. Under a program of the educational organization that is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet needs where services provided by the students (or former students) are for or under the direction of a governmental unit or a tax-exempt section 501(c)(3) organization.

Special rule for student loan discharges for 2021 through 2025. The American Rescue Plan Act of 2021 modified the treatment of student loan forgiveness for discharges in 2021 through 2025. Generally, if you're responsible for making loan payments, and the loan is canceled or repaid by someone else, you must include the amount that was canceled or paid on your behalf in your gross income for tax purposes. However, in certain circumstances you may be able to exclude this amount from gross income if the loan was one of the following.

- A loan for postsecondary educational expenses.
- A private education loan.
- A loan from an educational organization described in section 170(b)(1)(A)(ii).
- A loan from an organization exempt from tax under section 501(a) to refinance a student loan.

See Pubs. 4681 and 970 for further details.

Loan for postsecondary educational expenses. This is any loan provided expressly for postsecondary education, regardless of whether provided through the educational organization or directly to the borrower, if such loan was made, insured, or guaranteed by one of the following.

- The United States, or an instrumentality or agency thereof.
- A state or territory of the United States; or the District of Columbia; or any political subdivision thereof.
- An eligible educational organization.

Eligible educational organization. An eligible educational organization is generally any accredited public, nonprofit, or proprietary (privately owned profit-making) college, university, vocational school, or other postsecondary educational organization.

Also, the organization must be eligible to participate in a student aid program administered by the U.S. Department of Education.

An eligible educational organization also includes certain educational organizations located outside the United States that are eligible to participate in a student aid program administered by the U.S. Department of Education.



The educational organization should be able to tell you if it is an eligible educational organization.

Private education loan. A private education loan is a loan provided by a private educational lender that:

- Is not made, insured, or guaranteed under Title IV of the Higher Education Act of 1965; and

- Is issued expressly for postsecondary educational expenses to a borrower, regardless of whether the loan is provided through the educational organization that the student attends or directly to the borrower from the private educational lender. A private education loan does not include an extension of credit under an open end consumer credit plan, a reverse mortgage transaction, a residential mortgage transaction, or any other loan that is secured by real property or a dwelling.

Private educational lender. A private educational lender is one of the following.

- A financial institution that solicits, makes, or extends private education loans.
- A federal credit union that solicits, makes, or extends private education loans.

- Any other person engaged in the business of soliciting, making, or extending private education loans.



The cancellation of your loan won't qualify for tax-free treatment if it is canceled because of services you performed for the private educational lender that made the loan or other organization that provided the funds.

Loan from an educational organization described in section 170(b)(1)(A)(ii).

This is any loan made by the organization if the loan is made:

- As part of an agreement with an entity described earlier under which the funds to make the loan were provided to the educational organization; or
- Under a program of the educational organization that is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet

needs where the services provided by the students (or former students) are for or under the direction of a governmental unit or a tax-exempt section 501(c)(3) organization.

Educational organization described in section 170(b)(1)(A)(ii). This is an educational organization that maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where it carries on its educational activities.



The cancellation of your loan won't qualify for tax-free treatment if it was made by an educational organization, a tax-exempt section 501(c)(3) organization, or a private education lender (as defined in section 140(a)(7) of the Truth in Lending Act) and was canceled because of the services you performed for either such organization or private education lender. See Exception, later.

Section 501(c)(3) organization. This is any corporation, community chest, fund, or foundation organized and operated exclusively for one or more of the following purposes.

- Charitable.
- Religious.
- Educational.
- Scientific.
- Literary.
- Testing for public safety.
- Fostering national or international amateur sports competition (but only if none of its activities involve providing athletic facilities or equipment).
- The prevention of cruelty to children or animals.

Exception. In most cases, the cancellation of a student loan made by an educational organization because of services you performed for that organization or another organization that provided the funds for the loan must be included in gross income on your tax return.

Refinanced loan. If you refinanced a student loan with another loan from an eligible educational organization or a tax-exempt organization, that loan may also be considered as made by a qualified lender. The refinanced loan is considered made by a qualified lender if it's made under a program of the refinancing organization that is designed to encourage students to serve in occupations with unmet needs or in areas with unmet needs where the services required of the students are for or under the direction of a governmental unit or a tax-exempt section 501(c)(3) organization.

Student loan repayment assistance.

Student loan repayments made to you are tax free if you received them for any of the following.

- The National Health Service Corps (NHSC) Loan Repayment Program.
- A state education loan repayment program eligible for funds under the Public Health Service Act.
- Any other state loan repayment or loan forgiveness program that is intended to provide for the increased availability of health services in underserved or health professional shortage areas (as determined by such state).



You can't deduct the interest you paid on a student loan to the extent payments were made through your participation in any of the above programs.

Deductible debt. You don't have income from the cancellation of a debt if your payment of the debt would be deductible. This exception applies only if you use the cash method of accounting. For more information, see chapter 5 of Pub. 334.

Price reduced after purchase. In most cases, if the seller reduces the amount of debt you owe for property you purchased, you don't have income from the reduction. The reduction of the debt is treated as a purchase price adjustment and reduces your basis in the property.

Excluded debt. Don't include a canceled debt in your gross income in the following situations.

- The debt is canceled in a bankruptcy case under title 11 of the U.S. Code.
See Pub. 908.

- The debt is canceled when you're insolvent. However, you can't exclude any amount of canceled debt that is more than the amount by which you're insolvent. See Pub. 908.
- The debt is qualified farm debt and is canceled by a qualified person. See chapter 3 of Pub. 225.
- The debt is qualified real property business debt. See chapter 5 of Pub. 334.
- The cancellation is intended as a gift.
- The debt is qualified principal residence indebtedness, discussed next.

Qualified principal residence

indebtedness (QPRI). This is debt secured by your principal residence that you took out to buy, build, or substantially improve your principal residence. QPRI can't be more than the cost of your principal residence plus improvements.

You must reduce the basis of your principal residence by the amount excluded from gross income. To claim the exclusion, you must file Form 982 with your tax return.

Principal residence. Your principal residence is the home where you ordinarily live most of the time. You can have only one principal residence at any one time.

Amount eligible for exclusion. The exclusion applies only to debt discharged after 2006 and in most cases before 2026. The maximum amount you can treat as QPRI is \$750,000 (\$375,000 if married filing separately). You can't exclude debt canceled because of services performed for the lender or on account of any other factor not directly related to a decline in the value of your residence or to your financial condition.

Limitation. If only part of a loan is QPRI, the exclusion applies only to the extent the canceled amount is more than the amount of the loan immediately before the cancellation that isn't QPRI.

Example 24. You file a joint return. Your principal residence is secured by a debt of \$900,000, of which \$700,000 is QPRI. Your residence is sold for \$600,000 and \$300,000 of debt is canceled. Only \$100,000 of the canceled debt may be excluded from income (the \$300,000 that was discharged minus the \$200,000 of nonqualified debt).

Forgiveness of Paycheck Protection

Program (PPP) loans. The forgiveness of a PPP loan creates tax-exempt income, so although you don't need to report the income from the forgiveness of your PPP loan on Form 1040 or 1040-SR, you do need to report certain information related to your PPP loan.

Revenue Procedure 2021-48, 2021-49 I.R.B. 835, permits taxpayers to treat tax-exempt income resulting from the forgiveness of a PPP loan as received or accrued (1) as, and to the extent that, eligible expenses are paid or incurred; (2) when you apply for forgiveness of the PPP loan; or (3) when forgiveness of the PPP loan is granted. If you have tax-exempt income resulting from the forgiveness of a PPP loan, attach a statement to your return reporting each taxable year for which you're applying Revenue Procedure 2021-48, and which section of Revenue Procedure 2021-48 you're applying—either section 3.01(1), (2), or (3). Any statement should include the following information for each PPP loan.

1. Your name, address, and ITIN or SSN;
2. A statement that you're applying or applied section 3.01(1), (2), or (3) of Revenue Procedure 2021-48, and for what taxable year;

3. The amount of tax-exempt income from forgiveness of the PPP loan that you're treating as received or accrued and for what taxable year; and
4. Whether forgiveness of the PPP loan has been granted as of the date you file your return.

Write "RP 2021-48" at the top of your attached statement.

Host

If you host a party or event at which sales are made, any gift or gratuity you receive for giving the event is a payment for helping a direct seller make sales. You must report this item as income at its FMV.

Your out-of-pocket party expenses are subject to the 50% limit for meal expenses. For tax years beginning after 2017, no deduction is allowed for any expenses related to activities generally considered entertainment, amusement, or recreation.

Taxpayers may continue to deduct 50% of the cost of business meals if the taxpayer (or an employee of the taxpayer) is present and the food or beverages aren't considered lavish or extravagant. The meals may be provided to a current or potential business customer, client, consultant, or similar business contact. Food and beverages that are provided during entertainment events won't be considered entertainment if purchased separately from the event.

For more information about the limit for meal expenses, see *50% Limit* in Pub. 463.

Life Insurance Proceeds

Life insurance proceeds paid to you because of the death of the insured person aren't taxable unless the policy was turned over to you for a price. This is true even if the proceeds were paid under an accident or health insurance policy or an endowment contract issued on or before December 31, 1984.

However, interest income received as a result of life insurance proceeds may be taxable.

Proceeds not received in installments. If death benefits are paid to you in a lump sum or other than at regular intervals, include in your income only the benefits that are more than the amount payable to you at the time of the insured person's death. If the benefit payable at death isn't specified, you include in your income the benefit payments that are more than the present value of the payments at the time of death.

Proceeds received in installments. If you receive life insurance proceeds in installments, you can exclude part of each installment from your income.

To determine the excluded part, divide the amount held by the insurance company (generally, the total lump sum payable at the death of the insured person) by the number of installments to be paid.

Include anything over this excluded part in your income as interest.

Example 25. The face amount of the policy is \$75,000 and, as beneficiary, you choose to receive 120 monthly installments of \$1,000 each. The excluded part of each installment is \$625 ($\$75,000 \div 120$), or \$7,500 for an entire year. The rest of each payment, \$375 a month (or \$4,500 for an entire year), is interest income to you.

Installments for life. If, as the beneficiary under an insurance contract, you're entitled to receive the proceeds in installments for the rest of your life without a refund or period-certain guarantee, you figure the excluded part of each installment by dividing the amount held by the insurance company by your life expectancy. If there is a refund or period-certain guarantee, the amount held by the insurance company for this purpose is reduced by the actuarial value of the guarantee.

Surviving spouse. If your spouse died before October 23, 1986, and insurance proceeds paid to you because of the death of your spouse are received in installments, you can exclude up to \$1,000 a year of the interest included in the installments. If you remarry, you can continue to take the exclusion.

Employer-owned life insurance contract.

If you're the policyholder of an employer-owned life insurance contract, you must include in income any life insurance proceeds received that are more than the premiums and any other amounts you paid on the policy. You're subject to this rule if you have a trade or business, you own a life insurance contract on the life of your employee, and you (or a related person) are a beneficiary under the contract.

However, you may exclude the full amount of the life insurance proceeds if the following apply.

1. Before the policy is issued, you provide written notice about the insurance to the employee and the employee provides written consent to be insured.
2. Either:
 - a. The employee was your employee within the 12-month period before death, or, at the time the contract was issued, was a director or highly compensated employee; or
 - b. The amount is paid to the family or designated beneficiary of the employee.

Interest option on insurance. If an insurance company pays you interest only on proceeds from life insurance left on deposit, the interest you're paid is taxable.

If your spouse died before October 23, 1986, and you chose to receive only the interest from your insurance proceeds,

the \$1,000 interest exclusion for a surviving spouse doesn't apply. If you later decide to receive the proceeds from the policy in installments, you can take the interest exclusion from the time you begin to receive the installments.

Surrender of policy for cash. If you surrender a life insurance policy for cash, you must include in income any proceeds that are more than the cost of the life insurance policy. In most cases, your cost (or investment in the contract) is the total of premiums that you paid for the life insurance policy, less any refunded premiums, rebates, dividends, or unrepaid loans that weren't included in your income.

You should receive a Form 1099-R showing the total proceeds and the taxable part. Report these amounts on lines 5a and 5b of Form 1040 or 1040-SR.



For information on when the proceeds are excluded from income, see Accelerated Death Benefits, later.

Split-dollar life insurance. In most cases, a split-dollar life insurance arrangement is an arrangement between an owner and a nonowner of a life insurance contract under which either party to the arrangement pays all or part of the premiums, and one of the parties paying the premiums is entitled to recover all or part of those premiums from the proceeds of the contract. There are two mutually exclusive rules to tax split-dollar life insurance arrangements.

1. Under the economic benefit rule, the owner of the life insurance contract is treated as providing current life insurance protection and other taxable economic benefits to the nonowner of the contract.

2. Under the loan rule, the nonowner of the life insurance contract is treated as loaning premium payments to the owner of the contract.

Only one of these rules applies to any one policy. For more information, see sections 1.61-22 and 1.7872-15 of the regulations.

Endowment Contract Proceeds

An endowment contract is a policy under which you're paid a specified amount of money on a certain date unless you die before that date, in which case the money is paid to your designated beneficiary.

Endowment proceeds paid in a lump sum to you at maturity are taxable only if the proceeds are more than the cost (investment in the contract) of the policy. To determine your cost, subtract any amount that you previously received under the contract and excluded from your income from the total premiums

(or other consideration) paid for the contract. Include the part of the lump payment that is more than your cost in your income.

Endowment proceeds that you choose to receive in installments instead of a lump sum payment at the maturity of the policy are taxed as an annuity. This is explained in Pub. 575. For this treatment to apply, you must choose to receive the proceeds in installments before receiving any part of the lump sum. This election must be made within 60 days after the lump-sum payment first becomes payable to you.

Accelerated Death Benefits

Certain amounts paid as accelerated death benefits under a life insurance contract or viatical settlement before the insured's death are excluded from income if the insured is terminally or chronically ill.

Viatical settlement. This is the sale or assignment of any part of the death benefit under a life insurance contract to a viatical settlement provider. A viatical settlement provider is a person who regularly engages in the business of buying or taking assignment of life insurance contracts on the lives of insured individuals who are terminally or chronically ill and who meets the requirements of section 101(g)(2)(B) of the Internal Revenue Code.

Exclusion for terminal illness. Accelerated death benefits are fully excludable if the insured is a terminally ill individual.

This is a person who has been certified by a physician as having an illness or physical condition that can reasonably be expected to result in death within 24 months from the date of the certification.

Exclusion for chronic illness. If the insured is a chronically ill individual who isn't terminally ill,

accelerated death benefits paid on the basis of costs incurred for qualified long-term care services are fully excludable. Accelerated death benefits paid on a per diem or other periodic basis are excludable up to a limit. For 2024, this limit is \$410. It applies to the total of the accelerated death benefits and any periodic payments received from long-term care insurance contracts. For information on the limit and the definitions of chronically ill individual, qualified long-term care services, and long-term care insurance contracts, see *Long-Term Care Insurance Contracts* under *Sickness and Injury Benefits*, earlier.

Exception. The exclusion doesn't apply to any amount paid to a person (other than the insured) who has an insurable interest in the life of the insured because the insured:

- Is a director, officer, or employee of the person; or
- Has a financial interest in the person's business.

Form 8853. To claim an exclusion for accelerated death benefits made on a per diem or other periodic basis, you must file Form 8853 with your return. You don't have to file Form 8853 to exclude accelerated death benefits paid on the basis of actual expenses incurred.

Recoveries

A recovery is a return of an amount you deducted or took a credit for in an earlier year. The most common recoveries are refunds, reimbursements, and rebates of itemized deductions. You may also have recoveries of nonitemized deductions (such as payments on previously deducted bad debts) and recoveries of items for which you previously claimed a tax credit.

Tax benefit rule. You must include a recovery in your income in the year you receive it up to the amount by which the deduction or credit you took for the recovered amount reduced your tax in the earlier year.

For this purpose, any increase to an amount carried over to the current year that resulted from the deduction or credit is considered to have reduced your tax in the earlier year.

Federal income tax refund. Refunds of federal income taxes aren't included in your income because they're never allowed as a deduction from income.

State tax refund. If you received a state or local income tax refund (or credit or offset) in 2024, you must generally include it in income if you deducted the tax in an earlier year. The payer should send Form 1099-G to you by January 31, 2025. The IRS will also receive a copy of the Form 1099-G. If you file Form 1040 or 1040-SR, use the worksheet in the 2024 Instructions for Schedule 1 (Form 1040) to figure the amount (if any) to include in your income. See *Itemized Deduction Recoveries*, later, for when you must use Worksheet 2, later in this publication.

If you could choose to deduct for a tax year either:

- State and local income taxes, or
- State and local general sales taxes, then the maximum refund that you may have to include in income is limited to the excess of the tax you chose to deduct for that year over the tax you didn't choose to deduct for that year.

Example 26. For 2023, you can choose a \$10,000 state income tax deduction or a \$9,000 state general sales tax deduction. You choose to deduct the state income tax. In 2024, you receive a \$2,500 state income tax refund. The maximum refund that you may have to include in income is \$1,000, because you could have deducted \$9,000 in state general sales tax.

Example 27. For 2023, you can choose a \$9,500 state general sales tax deduction based on actual expenses or a \$9,200 state income tax deduction. You choose to deduct the general sales tax deduction. In 2024, you return an item you had purchased and receive a \$500 sales tax refund. In 2024, you also receive a \$1,500 state income tax refund. The maximum refund that you may have to include in income is \$500, because it's less than the excess of the tax deducted (\$9,500) over the tax you didn't choose to deduct ($\$9,200 - \$1,500 = \$7,700$). Because you didn't choose to deduct the state income tax, you don't include the state income tax refund in income.

Mortgage interest refund. If you received a refund or credit in 2024 of mortgage interest paid in an earlier year, the amount should be shown in Form 1098, box 4. Don't subtract the refund amount from the interest you paid in 2024.

You may have to include it in your income under the rules explained in the following discussions.

Interest on recovery. If you receive interest on any of the amounts you recover, this interest must be reported as interest income in the year received. For example, report any interest you received on state or local income tax refunds on Form 1040, 1040-SR, or 1040-NR, line 2b.

Recovery and expense in same year.

If the refund or other recovery and the expense occur in the same year, the recovery reduces the deduction or credit and isn't reported as income.

Recovery for 2 or more years. If you receive a refund or other recovery that is for amounts you paid in 2 or more separate years, you must allocate, on a pro rata basis, the recovered amount between the years in which you paid it.

This allocation is necessary to determine the amount of recovery from any earlier years and to determine the amount, if any, of your allowable deduction for this item for the current year.

Example 28. You paid 2023 estimated state income tax of \$4,000 in four equal payments. You made your fourth payment in January 2024. You had no state income tax withheld during 2023. In 2024, you received a \$400 tax refund based on your 2023 state income tax return. You claimed itemized deductions each year on Schedule A (Form 1040).

You must allocate the \$400 refund between 2023 and 2024, the years in which you paid the tax on which the refund is based. You paid 75% ($\$3,000 \div \$4,000$) of the estimated tax in 2023, so 75% of the \$400 refund, or \$300, is for amounts you paid in 2023 and is a recovery item.

If all of the \$300 is a taxable recovery item, you'll include \$300 on Schedule 1 (Form 1040), line 1, for 2024, and attach a copy of your calculation showing why that amount is less than the amount shown on the Form 1099-G you received from the state.

The balance (\$100) of the \$400 refund is for your January 2024 estimated tax payment. When you figure your deduction for state and local income taxes paid during 2024, you'll reduce the \$1,000 paid in January by \$100. Your deduction for state and local income taxes paid during 2024 will include the January net amount of \$900 (\$1,000 – \$100), plus any estimated state income taxes paid in 2024 for 2024, and any state income tax withheld during 2024.

Joint state or local income tax return. If you filed a joint state or local income tax return in an earlier year and you aren't filing a joint Form 1040 or 1040-SR with the same person for 2024,

any refund of a deduction claimed on that state or local income tax return must be allocated to the person that paid the expense. If both persons paid a portion of the expense, allocate the refund based on your individual portion. For example, if you paid 25% of the expense, then you would use 25% of the refund to figure if you must include any portion of the refund in your income.

Registered domestic partners (RDPs) domiciled in community property states.

For the rules that apply to RDPs who are domiciled in community property states, see Pub. 555 and Form 8958.

Deductions not itemized. If you didn't itemize deductions for the year for which you received the recovery of an expense that was deductible only if you itemized, don't include any of the recovery amount in your income.

Example 29. You claimed the standard deduction on your 2023 federal income tax return. In 2024, you received a refund of your 2023 state income tax. Don't report any of the refund as income because you didn't itemize deductions for 2023.

Itemized Deduction Recoveries

The following discussion explains how to determine the amount to include in your income from a recovery of an amount deducted in an earlier year as an itemized deduction. However, you generally don't need to use this discussion if you file Form 1040 or 1040-SR and the recovery is for state or local income taxes paid in 2023. Instead, use the State and Local Income Tax Refund Worksheet—Schedule 1, Line 1, in the 2024 Instructions for Schedule 1 (Form 1040) for line 1 to figure the amount (if any) to include in your income. See the Instructions for Forms 1040 and 1040-SR.

You can't use the State and Local Income Tax Refund Worksheet—Schedule 1, Line 1, and must use this discussion if you're a nonresident alien (discussed later) or any of the following statements are true.

1. You received a refund in 2024 that is for a tax year other than 2023.
2. You received a refund other than an income tax refund, such as a general sales tax or real property tax refund, in 2024 of an amount deducted or credit claimed in an earlier year.
3. The amount on your 2023 Form 1040, line 13, was more than the amount on your 2023 Form 1040, line 11 minus line 12.
4. You had taxable income on your 2023 Form 1040, line 15, but no tax on your Form 1040, line 16, because of the 0% tax rate on net capital gains and

qualified dividends in certain situations. See Capital gains, later.

5. Your 2023 state and local income tax refund is more than your 2023 state and local income tax deduction minus the amount you could have deducted as your 2023 state and local general sales taxes.
6. You made your last payment of 2023 estimated state or local income tax in 2024.
7. You owed AMT in 2023.
8. You couldn't use the full amount of credits you were entitled to in 2023 because the total credits were more than the amount shown on your 2023 Form 1040, line 18.
9. You could be claimed as a dependent by someone else in 2023.

10. You received a refund because of a jointly filed state or local income tax return, but you aren't filing a joint 2024 Form 1040 or 1040-SR with the same person.



If you also recovered an amount deducted as a nonitemized deduction, figure the amount of that recovery to include in your income and add it to your adjusted gross income (AGI) before applying the rules explained here. See Nonitemized Deduction Recoveries, later.

Nonresident aliens. If you're a nonresident alien and file Form 1040-NR, you can't claim the standard deduction. If you recover an itemized deduction that you claimed in an earlier year, you must generally include the full amount of the recovery in your income in the year you receive it. However, if you had no taxable income in that earlier year (see Negative taxable income, later),

you should complete Worksheet 2 to determine the amount you must include in income. If any other statement under *Total recovery included in income*, later, isn't true, see the discussion referenced in the applicable statement to determine the amount to include in income.

Capital gains. If you determined your tax in the earlier year by using the Schedule D Tax Worksheet, or the Qualified Dividends and Capital Gain Tax Worksheet, and you receive a refund in 2024 of a deduction claimed in that year, you'll have to refigure your tax for the earlier year to determine if the recovery must be included in your income. If inclusion of the recovery doesn't change your total tax, you don't include the recovery in income. However, if your total tax increases by any amount, you must include the recovery in your income up to the amount of the deduction that reduced your tax in the earlier year.