Instructions for Schedule D (Form 1065)

Capital Gains and Losses

What's New
An additional entry section has been added to line 1 and line 7 so that up to 5 capital gain or loss transactions can be entered on these lines. If you need to list more than 5 transactions for these lines, you may use Schedule D-1, Continuation Sheet for Schedule D (Form 1065, 1065-B, or 8865), to report the additional transactions. On Schedule D, line 2 and line 8 are now used to enter the total amounts from the applicable column (f) of Schedule D-1.

Note. An electronically filed Schedule D (Form 1065) is able to accommodate the reporting of more than 5 capital gain or loss transactions. If the partnership e-files its return and includes its transactions on the electronic short-term capital gain (loss) or long-term capital gain (loss) lines, it is not necessary to complete Schedule D-1 (Form 1065).

Purpose of Schedule
Use Schedule D (Form 1065) to report sales or exchanges of capital assets, capital gain distributions, and nonbusiness bad debts. Do not report on Schedule D capital gains (losses) specially allocated to any partners.

Enter capital gains (losses) specially allocated to the partnership as a partner in other partnerships and from estates and trusts on Schedule D, line 5 or 11, whichever applies. Enter capital gains (losses) of the partnership that are specially allocated to partners directly on line 8, 9a, or 11 of Schedule K. See How Income Is Shared Among Partners in the Instructions for Form 1065 for more information.

Note. For more information, see Pub. 544, Sales and Other Dispositions of Assets.

Other Forms The Partnership May Have To File
Use Form 4797, Sales of Business Property, to report:

• Sales or exchanges of property used in a trade or business.

• Stock in trade or other property included in inventory or held mainly for sale to customers.

• Accounts or notes receivable acquired in the ordinary course of the trade or business for services rendered or from the sale of stock in trade or other property held mainly for sale to customers.

• Certain commodities derivative financial instruments held by a dealer. See section 1221(a)(6).

• Certain hedging transactions entered into in the normal course of the trade or business. See section 1221(a)(7).

• Supplies regularly used in the trade or business.

Items for Special Treatment

• Transactions by a securities dealer. See section 1236.

• Bonds and other debt instruments. See Pub. 550, Investment Income and Expenses.

• Certain real estate subdivided for sale that may be considered a capital asset. See section 1237.

• Gain on the sale of depreciable property to a more than 50%-owned entity, or to a trust in which the partnership is a beneficiary, is treated as ordinary gain.

• Liquidating distributions from a corporation. See Pub. 550 for details.

• Gain on the sale or exchange of stock in certain foreign corporations. See section 1248.

• Gain or loss on options to buy or sell, including closing transactions. See Pub. 550 for details.

• Gain or loss from a short sale of property. See Pub. 550 for details.

• Transfer of property to a political organization if the fair market value (FMV) of the property exceeds the partnership's adjusted basis in such property. See section 887.

• Any loss on the disposition of converted wetland or highly erodible cropland that is first used for farming after March 1, 1986, is reported as a long-term capital loss on Schedule D, but any gain on such a disposition is reported as ordinary income on Form 4797. See section 1257 for details.

• Transfer of partnership assets and liabilities to a newly formed corporation in exchange for all of its stock. See Rev. Rul. 84-111, 1984-2 C.B. 88.

• Disposition of foreign investment in a U.S. real property interest. See section 887.

• Any loss from a sale or exchange of property between the partnership and certain related persons is not allowed, except for distributions in a complete
liquidation of a corporation. See sections 267 and 707(b) for details. Any loss from the loss that are capital assets that become worthless during the year is treated as a loss from the sale or exchange of a capital asset on the last day of the applicable tax year.

- Nonrecognition of gain on sale of stock to an employee stock ownership plan (ESOP) or an eligible cooperative. See section 1042 and Temporary Regulations section 1.1042-1T for rules under which the partnership may elect not to recognize gain from the sale of certain stock to an ESOP or an eligible cooperative.

- A nonbusiness bad debt must be treated as a short-term capital loss. A debt that is specially allocated among the principal contract, or a futures or forward contract must be treated as a short-term capital loss. The rules for investor and trader must be treated in a similar manner. If a short-term capital loss is any long-term gain or investment. The rules for investors of the partnership's trade or business. A trader may hold securities for a short-term capital loss. See section 1260 for details.

- Gain from certain constructive ownership transactions. Gain in excess of the gain that would have been recognized if the partnership had held a financial asset directly during the term of the derivative contract must be treated as ordinary income. See section 1260 for details.

- Gain from the sale of collectibles. Any loss from a wash sale of stock or securities that are capital assets when figured net earnings from the share of income or capital gain that is not specially allocated among the principal contract must be treated as ordinary income. See section 1260 for details.

- Gain from installment sales. If the partnership held the appreciated asset when the partnership's activity is a business: “short sale against the box.” Generally, constructive sale of an appreciated asset when it (or a related person, in some cases) does one of the following:

- Enters into an offsetting notional principal contract relating to the same or substantially identical property (that is, a short-sale against the box).

- Enters into a futures or forward contract to deliver the same or substantially identical property (that is, a short-sale against the box).

- Enters into a futures or forward contract to deliver the same or substantially identical property (that is, a short-sale against the box).
throughout the 60-day period starting on the date the transaction was closed, and
• At no time during that 60-day period was the partnership’s risk of loss reduced by holding certain other positions.

For details and other exceptions to the rules, see Pub. 550.

Rollover of gain from qualified stock.
If the partnership sold qualified small business stock (defined below) it held for more than 6 months, it may postpone gain if it purchased other qualified small business stock during the 60-day period that began on the date of the sale. The partnership must recognize gain to the extent the sale proceeds exceed the cost of the replacement stock. Reduce the basis of the replacement stock by any postponed gain.

If the partnership chooses to postpone gain, report the entire gain realized on the sale on line 1 or 7. Directly below the line on which the partnership reported the gain, enter in column (a) “Section 1045 Rollover” and in column (f) the amount of the postponed gain.

Attach a statement to Form 1065 that identifies the replacement qualified small business stock, shows the computation of the adjustment to the partnership’s basis in the replacement stock for the amount of any postponed gain under section 1045, and shows the dates on which the replacement stock was acquired by the partnership.

The partnership also must separately state the amount of the rollover gain over qualified stock under section 1045 on Form 1065, Schedule K, line 11. Each partner must determine if he or she qualifies for the rollover at the partner level or if he or she wants to opt out of the section 1045 election. The partnership must separately state on that line (and not on Schedule D) any gain that would qualify for the section 1045 rollover at the partner level instead of the partnership level (because a partner was entitled to purchase replacement stock) and any gain on qualified stock that could qualify for the partial exclusion under section 1202.

To be qualified small business stock, the stock must meet all of the following tests.
• It must be stock in a C corporation (that is, not S corporation stock).
• It must have been originally issued after August 10, 1993.
• As of the date the stock was issued, the corporation was a qualified small business. A qualified small business is a domestic C corporation with total gross assets of $50 million or less (a) at all times after August 9, 1993, and before the stock was issued and (b) immediately after the stock was issued. Gross assets include those of any predecessor of the corporation. All corporations that are members of the same parent-subsidiary controlled group are treated as one corporation.
• The partnership must have acquired the stock at its original issue (either directly or indirectly under a partnership or otherwise) in exchange for money or other property or as pay for services (other than as an underwriter) to the corporation. In certain cases, the partnership may meet the test if it acquired the stock from another person who met this test (such as by gift or at a discount) or through a contribution or exchange of qualified business stock by the holder.
• During substantially all the time the partnership held the stock:
  1. The corporation was a C corporation,
  2. At least 80% of the value of the corporation’s assets were used in the active conduct of one or more qualified businesses (defined below), and
  3. The corporation was not a foreign corporation, domestic international sales corporation (DISC), former DISC, corporation that has made (or that has a subsidiary that has made) a section 936 election, regulated investment company (RIC), real estate investment trust (REIT), real estate mortgage investment conduit (REMIC), financial asset securitization investment trust (FASIT), or cooperative.

Note. A specialized small business investment company (SSBIC) is treated as having met test 2 above.

A qualified business is any business other than the following.
• One involving services performed in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage services.
• One whose principal asset is the reputation or skill of one or more employees.
• Any banking, insurance, financing, leasing, investing, or similar business.
• Any farming business (including the raising or harvesting of trees).
• Any business involving the production of products for which percentage depletion can be claimed.
• Any business of operating a hotel, motel, restaurant, or similar business.

Rollover of gain from empowerment zone assets.
If the partnership sold or exchanged a District of Columbia Enterprise Zone (DC Zone) asset that it held for more than 5 years, it may postpone the gain. The DC Zone asset must have been acquired by the partnership, which is a DC Zone business, after August 9, 1993, and before 2010, to qualify as an asset for which the partnership may be able to take the exclusion. The sale or exchange of DC Zone capital assets reported on Schedule D includes:
• Stock in a domestic corporation that was a DC Zone business.
• Interest in a partnership that was a DC Zone business.
• The sale or exchange of property used in the partnership’s DC Zone business on Form 4797.

Gains not qualified for exclusion.
The following gains do not qualify for the exclusion of gain from DC Zone assets.
• Gain on the sale of an interest in a partnership, which is a DC Zone business, attributable to unrecovered section 1250 gain. See the instructions for line 9c of Schedule K for information on how to report unrecovered section 1250 gain.
• Gain on the sale of an interest in a partnership or S corporation attributable to real property or an intangible asset which is not an integral part of the DC Zone business.
• Gain from a related-party transaction. See Sales and Exchanges Between Related Persons in chapter 2 of Pub. 544.

Qualified capital gain.
Qualified capital gain is any gain recognized on the sale or exchange of a qualified community asset, but does not include any of the following.
• Gain treated as ordinary income under section 1245.
• Section 1250 gain figured as if section 1250 applied to all depreciation rather than the additional depreciation.
• Gain attributable to real property, or an intangible asset, that is not an integral part of a qualified community business.
• Gain from a related-party transaction. See Sales and Exchanges Between Related Persons in chapter 2 of Pub. 544.

How to report.
Report the entire gain realized from the sale or exchange as the partnership otherwise would report to the exclusion. On Schedule D, line 7, enter “Qualified Community Asset” in column (a) and enter as a (loss) in column (f) the amount of the allowable exclusion. If reporting the sale directly on Schedule D, line 7, use the line directly below the line the partnership is using to report the gain from the sale to report the exclusion.

Exclusion of gain from DC Zone assets.
If the partnership sold or exchanged a District of Columbia Enterprise Zone (DC Zone) asset that it held for more than 5 years, it may be able to exclude the qualified capital gain. The DC Zone asset must have been acquired after August 1997, but before 2010, to qualify as an asset for which the partnership may be able to take the exclusion. The sale or exchange of DC Zone capital assets reported on Schedule D includes:
• Stock in a domestic corporation that was a DC Zone business.
• Interest in a partnership that was a DC Zone business.

Report the sale or exchange of property used in the partnership’s DC Zone business on Form 4797.

Gains not qualified for exclusion.
The following gains do not qualify for the exclusion of gain from DC Zone assets.
• Gain on the sale of an interest in a partnership, which is a DC Zone business, attributable to unrecovered section 1250 gain. See the instructions for line 9c of Schedule K for information on how to report unrecovered section 1250 gain.
• Gain on the sale of an interest in a partnership or S corporation attributable to real property or an intangible asset which is not an integral part of the DC Zone business.
• Gain from a related-party transaction. See Sales and Exchanges Between Related Persons in chapter 2 of Pub. 544.
See Pub. 954 and section 1400B for more details on DC Zone assets and special rules.

**How to report.** Report the entire gain realized from the sale or exchange as the partnership otherwise would without regard to the exclusion. To report the exclusion, enter “DC Zone Asset Exclusion” on Schedule D, line 7, column (a) and enter as a (loss) in column (f) the amount of the exclusion.

**Specific Instructions**

**Columns (b) and (c). Date Acquired and Date Sold**

Use the trade dates for date acquired and date sold for stocks and bonds traded on an exchange or over-the-counter market. The acquisition date for an asset the partnership held on January 1, 2001, for which it made an election to recognize any gain on a deemed sale, is the date of the deemed sale and reacquisition.

**Column (d). Sales Price**

Enter in this column either the gross sales price or the net sales price from the sale. On sales of stocks and bonds, report the gross amount as reported to the partnership by the partnership’s broker on Form 1099-B, Proceeds From Broker and Barter Exchange Transactions, or similar statement. However, if the broker advised the partnership that gross proceeds (gross sales price) less commissions and option premiums were reported to the IRS, enter that net amount in column (d).

**Column (e). Cost or Other Basis**

In general, the cost or other basis is the cost of the property plus purchase commissions and improvements minus depletion. If the partnership got the property in a tax-free exchange, involuntary conversion, or wash sale of stock, it may not be able to use the actual cash cost as the basis. If the partnership does not use cash cost, attach an explanation of the basis.

If the partnership sold stock, adjust the basis by subtracting all the stock-related nontaxable distributions received before the sale. This includes nontaxable distributions from utility company stock and mutual funds. Also adjust the basis for any stock splits or stock dividends.

If the partnership elected to recognize gain on an asset held on January 1, 2001, its basis in the asset is its closing market price or FMV, whichever applies, on the date of the deemed sale and reacquisition, whether the deemed sale resulted in a gain or an allowed loss.

If a charitable contribution deduction is passed through to a partner because of a bargain sale of property to a charitable organization, the adjusted basis for determining gain from the sale is an amount that has the same ratio to the adjusted basis as the amount realized has to the FMV.

See section 852(f) for the treatment of certain load charges incurred in acquiring stock in a mutual fund with a reinvestment right.

If the gross sales price is reported in column (d), increase the cost or other basis by any expense of sale, such as broker’s fees, commissions, or option premiums, before making an entry in column (e).

For more details, see Pub. 551, Basis of Assets.

**Column (f). Gain or (Loss)**

Make a separate entry in this column for each transaction reported on lines 1 and 7 and any other line(s) that applies to the partnership. For lines 1 and 7, subtract the amount in column (e) from the amount in column (d). Enter negative amounts in parentheses.

**Lines 5 and 11. Capital Gains (Losses) From Other Partnerships, Estates, and Trusts**

See the Schedule K-1 or other information supplied to you by the other partnership, estate, or trust.

**Line 12. Capital Gain Distributions**

On line 12, column (f), report the total amount of (a) capital gain distributions and (b) the partnership’s share of undistributed capital gains from a RIC or REIT. Report the partnership’s share of taxes paid on undistributed capital gains by a RIC or REIT on a statement attached to Form 1065 for Schedule K, line 15f (and each partner’s share in box 15 of Schedule K-1 using code H).