



Instructions for Form 4952

Investment Interest Expense Deduction

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

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.

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

Recordkeeping	1 hr., 5 min.
Learning about the law or the form	22 min.
Preparing the form	1 hr., 6 min.
Copying, assembling, and sending the form to IRS	20 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form more simple, we would be happy to hear from you. You can write to both IRS and the Office of Management and Budget at the addresses listed in the instructions for the tax return with which this form is filed.

General Instructions

Purpose of Form

Interest expense paid by an individual, estate, or a trust on a loan that is allocable to property held for investment (defined below), may not be fully deductible in the current year. Form 4952 is used to figure the amount of investment interest expense deductible for the current year and the amount, if any, to carry forward to future years.

For more details, get **Pub. 550, Investment Income and Expenses**.

Who Must File

If you are an individual, estate, or a trust, and you claim a deduction for investment interest expense, you must complete and attach Form 4952 to your tax return, unless all of the following apply:

- your only investment income was from interest or dividends,
- you have no other deductible expenses connected with the production of interest or dividends,
- your investment interest expense is not more than your investment income,
- you have no carryovers of investment interest expense from 1989, and
- you have no passive activity losses.

Allocation of Interest Expense Under Temporary Regulations Section 1.163-8T.—If you paid or accrued interest on a loan and you used the proceeds of the loan

for more than one purpose, you may have to allocate the interest paid. This is necessary because of the different rules that apply to investment interest, personal interest, trade or business interest, home mortgage interest, and passive activity interest. See **Pub. 550**.

Specific Instructions

Line 1—Investment Interest Expense.—Enter the investment interest paid or accrued during the tax year, regardless of when the indebtedness was incurred. Include interest paid or accrued on a loan (or part of a loan) that is allocable to property held for investment.

Be sure to include investment interest expense reported to you on Schedule K-1 from a partnership, an S corporation, an estate, or a trust. 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 the following:

- home mortgage interest;
- interest expense that is properly allocable to a passive activity (see **Passive Activities** below);
- any interest expense that is capitalized, such as construction interest subject to section 263A; or
- interest expense relating to tax-exempt interest income under section 265.

Passive Activities. Investment interest expense does not include any interest expense that is taken into account in determining your income or loss from a passive activity. However, interest expense that is properly allocable to portfolio income is investment interest expense and is not taken into account when determining your income or loss from a passive activity. Portfolio income includes income (not derived in the ordinary course of a trade or business) from interest, dividends, annuities, royalties, and net gain from the disposition of property held for investment. See the instructions for Schedule E (Form 1040) for the definition of passive activity.

Line 2—Investment Income Reduced by Investment Expenses.—Figure your total gross investment income (defined below). Subtract your total investment expenses (defined below) from that total and enter the result on line 2. Be sure to take into account investment income and expenses reported to you on Schedule K-1 from a partnership, an S corporation, an estate, or a trust.

Investment Income. Investment income includes income (not derived in the ordinary course of a trade or business) from interest, dividends, annuities, royalties, and net gain from the disposition of property held for investment (including capital gain distributions from mutual funds). Net income from the following passive activities is also treated as investment income:

- (1) rental of substantially nondepreciable property;
- (2) equity-financed lending activities; and
- (3) acquisition of certain interests in a passthrough entity licensing intangible property.

See **Temporary Regulations** section 1.469-2T(f)(10) for details.

In addition to the activities listed above, net passive income from a passive activity of a publicly traded partnership (as defined in section 469(k)(2)) is also included in investment income. See **Notice 88-75, 1988-2 C.B. 386**, for details.

Investment income does not include Alaska Permanent Fund Dividends. See **Rev. Rul. 90-56, 1990-28 I.R.B. 6**.

Property Held for Investment. Property held for investment includes property that produces investment income. However, it does not include an interest in a passive activity. See **Passive Activities**, above, for more details.

Property held for investment also includes an interest in an activity of conducting a trade or business in which you did not materially participate and that is not a passive activity. For example, a working interest in an oil or gas property that is not a passive activity is property held for investment if you did not materially participate in the activity.

Investment Expenses. 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.

Investment expenses do not include any deductions taken into account in determining your income or loss from a passive activity.

If you have investment expenses that are included as a miscellaneous itemized deduction on line 21 of Schedule A (Form 1040), you may not have to use all of the amount for purposes of line 2 of Form 4952. The 2% adjusted gross income limitation on Schedule A may reduce the amount.

To figure the amount to use, compare the amount of the investment expenses included on line 21 of Schedule A with the total miscellaneous expenses on line 25 of Schedule A. The smaller of the investment expenses included on line 21 or the total of line 25 is the amount to use to figure the investment expense for line 2.

Example. Assume line 21 of Schedule A includes investment expenses of \$3,000, and line 25 is \$1,300 after the 2% adjusted gross income limitation. Investment expenses of \$1,300 are used to figure the amount of investment expense for line 2. If investment expenses of \$800 were included on line 21 and line 25 was \$1,300, investment expenses of \$800 would be used.

If you have investment expenses reported on a form or schedule other than Schedule A, include those expenses when figuring investment expenses for line 2.

Line 3—Phase-in of Passive Activity Losses.—Enter on this line any loss attributable to the phase-in allowed from a passive activity that is not a rental real estate activity with active participation.

Note: Form 8582, Passive Activity Loss Limitations, must be completed before you can get the figure for this line. See Computing Modified Adjusted Gross Income on Form 8582, below, to see if your allowable investment interest expense affects the computation of modified adjusted gross income for line 6 of Form 8582.

If you completed Form 8582, and line 2c of that form shows a loss and an amount is shown on line 15 of that form, you will have to include all or part of the amount from line 15 of Form 8582 on line 3 of Form 4952.

If you had a loss from a publicly traded partnership (PTP), include on line 3 of this form the loss attributable to the phase-in for each PTP. See example below.

If the amount on line 2c of Form 8582 is equal to or greater than the amount on line 12 of that form (treating both numbers as positive), all of the phase-in amount on line 15 is attributable to the amount on line 2c. Enter the entire amount from line 15 of Form 8582 on line 3 of this form.

If you have a loss on line 2c of Form 8582, as well as a loss attributable to rental real estate activities with active

participation shown on line 1c, you may use only part of the amount on line 15. Figure the amount by dividing line 2c by line 12 and multiplying line 15 by the result.

Example. Taxpayer A has a loss of (\$30,000) on line 1c and a loss of (\$50,000) on line 2c of Form 8582. Line 3 of Form 8582 shows a total loss of (\$80,000), and line 9 shows that the full \$25,000 special allowance was allowed. The loss attributable to the phase-in was computed on lines 10 through 15 of Form 8582 as follows:

10. Combine lines 1c and 2c	80,000
11. Special allowance	25,000
12. Subtract line 11 from line 10	55,000
13. Subtract line 9 from line 3 (80,000 - 25,000)	55,000
14. Enter the smaller of line 12 or line 13	55,000
15. Multiply line 14 by 10%	5,500

Taxpayer A figures the amount to enter on line 3 of Form 4952 as follows:

$$\frac{\text{line 2c}}{\text{line 12}} \times \text{line 15} = \text{phase-in adjustment for line 3 of Form 4952}$$

$$\frac{\$50,000}{\$55,000} \times \$5,500 = \$5,000$$

Taxpayer A would include \$5,000 on line 3 of Form 4952. If Taxpayer A also had a (\$3,500) pre-enactment loss from a PTP, the \$350 loss allowed for the PTP (\$3,500 x .1 = \$350) plus the \$5,000 would be entered on line 3.

Computing Modified Adjusted Gross Income on Form 8582.—To compute modified adjusted gross income on line 6 of Form 8582, you must know how much of your deductible investment interest expense is attributable to royalty income. Skip these instructions if you do not have interest expense attributable to royalties, or if line 2c of Form 8582 shows income or no entry.

If you have investment interest expense attributable to royalty income, and you also have a loss on line 2c of Form 8582, complete Form 4952 as you usually would, but enter -0- on line 3 of Form 4952. Use the allowable investment interest expense attributable to the royalty income that is included on that Form 4952 to figure gain or loss for purposes of modified adjusted gross

income on Form 8582. After completing Form 8582, refigure Form 4952 in the regular manner with the phase-in adjustment on line 3. Enter on Schedule E the allowable portion of investment interest expense attributable to the royalty income that is included on the refigured Form 4952.

Line 6—Investment Interest Expense.—Enter on line 6 the amount from line 1 minus any interest expense from a trade or business:

- (a) that is not a passive activity, and
- (b) in which you did not materially participate.

Line 7—Investment Income Reduced by Investment Expenses.—Enter on line 7 the amount from line 2 refigured without taking into account investment income or expenses from a trade or business:

- (a) that is not a passive activity, and
- (b) in which you did not materially participate.

Line 24.—This is your deductible investment interest expense.

Individuals. Enter the amount from line 24 on line 11 of Schedule A (Form 1040), even if all or part of it is attributable to a partnership or an S corporation. However, if any portion of this amount is attributable to royalties, enter that portion of the interest expense on Schedule E (Form 1040).

Estates and Trusts. Enter the amount from line 24 on line 10 of Form 1041.

Form 6198. If any portion of the deductible investment interest expense is attributable to an activity for which you are not at risk, you must also use Form 6198, At-Risk Limitations, to figure your deductible investment interest expense. Enter the portion attributable to the at-risk activity on line 4 of Form 6198. Reduce line 24 of Form 4952 by the amount entered on Form 6198. See Form 6198 and its instructions for more information, especially the instructions for line 4 of that form.

Alternative Minimum Tax. Deductible interest expense is an adjustment for alternative minimum tax purposes. Get Form 6251, Alternative Minimum Tax—Individuals, or Form 8656, Alternative Minimum Tax—Fiduciaries.

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