

## **TAX STATUTE OUTLINE**

### **Section 61 – Gross Income Defined**

- (a) Except as otherwise provided, GI means all income from whatever source derived including but not limited to:
- (1) Compensation for services including fees, commissions, fringe benefits, and similar items, (2) business income, (3) property gains, (4) interest, (5) rents, (6) royalties, (7) dividends, (8) alimony, (9) annuities, (10) life insurance and endowment, (11) pensions, (12) income from discharge of indebtedness, (13) P-ship share distribution, (14) income from decedent, and (15) income from estate or trust.

### **Section 119 – Meals or Lodging Furnished for the Convenience of ER**

- (a) These are excluded if furnished to EE, spouse, or dependents: IF
  - (1) Meals: are furnished on the premises
  - (2) Lodging: employee is required to accept the lodging on the premises as a condition of employment
- (b) (1) Convenience to the employer or whether the benefits are compensations are not determinative based on state statute or employment contract. (2) Charges for the meal and the fact that employee may accept or decline is not taken into account in determining the convenience. (3) (A) If employee must periodically pay a *fixed* charge for the meal and meals are for employer convenience and furnished by ER, then the *fixed* charge is excluded from the employee's gross income. (B) This is the case whether EE pays out of own funds or the charge is taken out of paycheck, and only if EE is required to pay it regardless of whether he accepts or declines the meal. (4) All meals furnished on the premises are treated as for the convenience of ER if more than half EE to whom such meals are furnished are for the convenience of ER.
- (d) (1) In the case of educational institutions, gross income does not include the value of qualified campus lodging to employees. (2) This does not apply to the excess of (A) either the lesser of 5% of the value of the lodging or the average rentals paid by non employee individuals comparable to the education housing, over (B) the rent paid by the employee.

Reg. 1.119-1

### **Section 132 – Certain Fringe Benefits**

- (a) Seven Exclusions
- (b) No-Additional Cost service defined: This is a service provided by Er to an ee for use by ee, if (1) service is offered for sale to customers in the ordinary course of business in which ee is providing services, and (2) the Er incurs no substantial additional cost (including forgone revenue) in providing the service to ee without regard to what ee pays.
- (c) Qualified ee Discount: (1) this relates to qualified property or services as long as the discount does not exceed (A) *for property*, gross percentage of the price at which it is offered by Er to customer, or (B) *for services*, 20% of the price.

- (2) Gross percentage profit: (A) this is the percent which (i) the excess of aggregate sales price of property sold by the employer to customers over the aggregate cost of the property to Er, is of (ii) the aggregate sale price of such property.
    - (B) Determination of gross profit percentage: this is determined by (i) all property offered to customers in the ordinary course of the line of business of the Er in which the ee is performing services and (ii) the Er's experience during the representative period.
  - (3) Employee Discount defined: This is the amount by which (A) the price at which the property/service are provided by the Er to the ee for use by such ee is less than (B) the price at which such property or services is offered by the Er to customers.
  - (4) qualified property or services: is any property other than property for investment or services that are offered for sale to the customer in the ordinary course of the line of business of the Er in which the ee is performing Services.
- (d) Working condition Fringe Defined: Any property/services provided to an ee of the Er to the extent that, if ee paid for is, it would be deductible under 162 or 167.
  - (e) De Minimis Fringe: (1) This is any property/service that has a value so small as to make accounting for it unreasonable or administratively impracticable.
    - Treatment of Certain Eating Facilities: The operation of any eating facility for ee is de minimis if (A) it is located on or near the business premises of Er and (B) the revenue derived from the facility normally equals or exceeds the direct operating cost of the facility.
  - (f) Qualified Transportation Fringe: (1) this means (A) transportation in a commuter highway vehicle is such transportation is in connection with travel between the residence and place of employment, (B) any transit pass, (C) qualified parking.
    - (2) the limitation is the amount of the fringe benefit provided by Er to ee and can be excluded but it cannot exceed (A) \$100/mo. in aggregate benefits, or (B) \$175 in qualified parking.
    - (3) there can be cash reimbursements. In the case of transit passes, this applies if there is a voucher which may be exchanged for a transit pass and is not available for direct distribution by Er to ee.
    - (4) There is no inclusion solely because the ee can choose between qualified transportation fringe and compensation which would otherwise be included in gross income.
    - (5) (A) a transit pass is a fare card, token, etc. that entitles someone to transportation if it is (i) on mass transit facilities, or (ii) provided by a person in the business of transporting persons for compensation if the vehicle seats at least 6 adults excluding the driver. (B) a commuter highway vehicle is that which (i) seats at least six adults not including the driver, (ii) at least 80% of the

mileage is from (I) purposes of transporting ee in connection with travel between residence and work, and (II) on trips during which the # of ee transported is at least ½ of the seating capacity. (C) Qualified parking means that which is provided to ee on or near the premises or on or near a location from which the ee commutes to work by transportation under transit pass section, commuter highway vehicle, or by carpool. This does not include any parking on or near property used by the ee for residential purposes.

- (h) Certain individuals treated as employees for purposes of subsection (a)(1) – no additional cost and (2) qualified employee discount includes
  - (1) retired and disabled employees and surviving spouses of ee treated as ee (A) separated from the line of business because of retirement or disability, and (B) widow or widower who died while employed in the line of business of while an ee within the meaning of someone who is disabled or retired.
  - (2) Spouse and dependent children (A) use by spouse or dependent children shall be treated as use by ee. (B) Dependent child means a child that (i) is dependent upon the ee or (ii) both of whose parents are deceased and has not reached the age of 25.
- (j)(1) Special Rules: Exclusions under no-additional cost and qualified ee discounts apply to highly compensated ee only if such fringe benefit is available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the Er which does not discriminate in favor of highly compensated ees.

#### **106(a) Contributions by employer to accident and health plans**

- a: ee gross income does not include employer-provided coverage under these plans.

#### **105(a) Amounts received under accident and health plans**

- a. Attributable to the employer: amounts received by an ee through accident/health insurance for personal injury or sickness are included in gross income if (1) they are attributable to contributions by Er not includible in the gross income of the ee, or (2) paid by Er.
- B. Amounts expended by medical care, gross income does not included subsection (a) if they are paid to taxpayer to reimburse the taxpayer from expenses incurred by him for medical care of taxpayer, spouse, and dependents. Medical care is defined in 213(d).
- C: Payments unrelated to absence from work is not included in gross income if the amounts (1) are payment for the permanent loss or loss of use of a member or function of the body, disfigurement or taxpayer, spouse or dependent, and (2) are computed with reference to the nature of the injury without regard to the period the ee is absent from work.

#### **213(d)(1) Definition of Medical Care:**

- A: This means the amount paid (A) for diagnosis, cure, mitigation, treatment, prevention, etc.

- B: Transportation primarily for and essential to medical care referred to in (A),
- C: Qualified long-term care services, OR
- D: Insurance covering care in (A) or (B). Only long-term care premiums of C are considered here.

**213(d)(9) – cosmetic surgery**

- A: Medical care does not cover this unless it is necessary to fix a deformity that relates to personal injury resulting from accident, trauma, or disfiguring disease.
- B: Cosmetic Surgery means a procedure that is directed at approving the appearance and does not promote the proper function of the body or prevent/treat illness/disease.

**162(l) – Special Rules for Health Insurance costs of Self-Employed individuals**

- If the person is an ee under 401(c)(1) then there is a deduction under this that equals the applicable % of the amount paid during the taxable year for insurance which constitutes medical car for the TP, spouse and dependents.

**Section 102**

A: Gross income does not include the value of property acquired by gift, bequest, devise or inheritance.

B: (1) The income from property in section A or (2) if that of A is income from property is not excluded. Paragraph 2 relates to that which is also made at intervals out of property.

C: Employee gifts: Subsection A does not include amounts transferred from employer to an employee.

**Section 274(b)**

(1) Limitations on gifts: Business expenses or business deductions do not allow for deductions as gifts that exceed more than \$25 per taxable year. This is a cumulative figure and does not pertain only to individual gifts. The gift here means that which the employee could exclude under 102.

- This does not include (A) items that cost the recipient less than \$4.00 with name permanently imprinted and one of a number of items typically distributed to recipient (business cards?). Or (B) a sign or display or promotional material to be displayed on the premises of the recipient.

(2) (A): The limitation in (1) in the case of a P-ship applies to the P-ship and to each member. (B) For purposes of (1) a husband and wife are treated as one taxpayer.

**Rule 117 – Qualified Scholarships**

- A: **General Rule:** Gross income does not include any amount, received, by individual, who is candidate for a degree, at an educational organization.
- B: **Qualified Scholarship:** (1) The individual must establish that the amount is used for qualified tuition and related expenses, (2) qualified tuition and related expenses mean (A) Tuition and feeds for the enrollment or attendance of a student at an educational institution, and (B) fees, books, supplies, equipment
- C: **Limitations:** (1) This does not include payment for services that is required as a condition for receiving the scholarship.
  - (2) **Exceptions:** Two specific scholarships relating to health professionals.

- **D: Qualified Tuition Reduction:** (1) this is not included in gross income. (2) this is the amount reduced from tuition given to ee of an educational institution below the graduate level. This includes family member 132(h).
  - (3): The reduction must not discriminate in favor of the highly compensated ee. It must be available on the same terms to each member of a group of ee.
- **E: Special Rules for Teaching and Research Assistants:** For graduate students of qualifying educational institutions who teach or do research, D2 does not place the limitation of “below the graduate level”. Any reduction is excluded.

**Rule 127(a), (c)(1), (c)(7) – Educational Assistance Programs**

- 127(a): (1) Gross income does not include amounts that the Er pays for educational assistances. (2) This only applies to the first \$5,250.00
- 127(c)(1): Educational Assistances means (A) payment by Er of expenses incurred by ee for education of ee. This includes, but is not limited to, tuition, fees, books, supplies, equipment, etc. (B) This does not included supplies that are retained after the completion, meals, lodging, transportation. This does not apply to payments involving sports, games or hobbies. But See 77.263.
- 127(c)(7): Disallowance of Excluded amounts as credit or deduction: EE cannot claim any credit or deduction under any other provision for any amount excluded from gross income in this section.

**Rule 61(a)(3):** Gross income includes gains derived from dealings in property.

**Rule 1001(a), (b) (c) – Determination of amount of and recognition of gain or loss:**

- (a): Gain *from sale or other disposition* is the excess of the amount realized over the adjusted basis. The loss is the excess of the adjusted basis over the amount realized.
- (b): The **amount realized** is the amount of money received plus the fair market value of the property (other than money) received.
- (c): Recognition of gain or loss: This includes the entire amount of the gain or loss.

**Rule 1011 – Adjusted Basis for Determining Gain or Loss**

- (a): This is the basis that is adjusted in 1016.
- (b): If there is a deduction under 170 (bargain sale to a charitable contribution), the gain is the portion of the adjusted basis which has the same ratio to the adjusted basis as the amount realized bears to the fair market value of the property.

**Rule 1012 – Basis of Property - cost**

- This is the cost of the property.

**Rule 1015(a); (d)(1) – Basis of Property Acquired by Gifts**

- **1015(a):** If something is acquired by gift then the basis is the same as it would be in the hands of the donor by whom did not acquire it by gift. But if the basis is greater than the FMV at the time of the gift, to determine the loss it shall be the FMV. If the facts regarding the extent of the gift are unknown to the donee, the

secretary shall try to find out. But if this is not possible, then the basis shall be the FMV at the date the secretary was acquired by the donor or last preceding owner.

- The gift must be acquired after 12/31/20
- **1015(d)(1):** (A) – for property acquired after 9/2/58, the basis is determined under (a) and increased by the amount of gift tax paid. The increase is not more than the FMV. (B) for property acquired before 9/2/58, and has not been sold, etc. the basis of the property is increased on the date by the amount of gift tax paid, but the increase shall not exceed the amount by which the FMV of the property at the time of the gift exceeded the basis of property in the hands of the donor at the time of the gift.

#### **1014(a)(1), (b)(1), (e) – Basis of Property Acquired from a Decedent**

- 1014(a)(1): The basis of property in the hands of a person that acquired it from a decedent or if the property passed from a decedent if the FMV of the property at the date of the death.
- 1014(b)(1): Examples of property that are deemed to have been acquired from or to have passed from the decedent are (1) bequest, devise, inheritance, from the estate.
- 1014(e): (1) In the case of a person dying after 12/31/81, the basis of property in the hands of the donor is the adjusted basis in the hands of the decedent immediately before death if (A) the appreciated property was acquired by the decedent during the one-year period ending on the date of the decedent's death, and (B) the property is acquired from the decedent by the donor of the property.
  - **Note:** The prevents manipulation of the tax benefits in the case of someone giving the decedent the property just before death and then taking the benefits upon the devise of the property back to the donor.
  - (2): Definitions (A): Appreciated property means any property if the FMV on the day it was transferred to decedent exceeds its adjusted basis. (B): Treatment of certain property sold by estate – Rules in (1)(A) apply to property sold by the estate or the trust of the decedent (if decedent was grantor) in the case that the donor was entitled to the proceeds of the sale.

#### **101(a) – Certain Death Benefits; Proceeds of Life Insurance Contracts Payable by Reason of Death**

- (1) Gross income does not include amounts received under a life insurance policy if “such amounts are paid by reason of the death of the insured.”
- (2) In a transfer for valuable consideration, the amount excluded from gross income in (1) shall not exceed an amount equal to the sum of the actual value of such consideration and the premiums and other amounts subsequently paid to the transferee.
  - This does not apply to a transfer (A) if there is a basis for determining the loss or gain in the hands of a transferee determined by reference to such basis of the contract or interest in the hands of the transferor OR (B) if the transfer is to the insured, partner of insured, partnership that insured belongs to, or corporation that insured is a shareholder or officer.

- The term other amounts includes interest paid or accrued by transferee on indebtedness if the interest paid or accrued is not allowable as deduction because of 264(a)(4)

**219(a)-(b)(1); 72(t)(1), (2)(A)(i), (iv), (2)(E) and (2)(F) – Retirement Savings**

- 219(a) Allowance of Deduction: If the case of individuals, there is a deduction equal to the qualified retirement contribution of the individual for the tax year.
- 219(b)(1) Max Amount of Deduction: The amount allowable as a deduction shall not exceed (A) the deductible amount, or (B) the amount equal to the compensation includible in the individual's gross income for the tax year.

**10-Percent Additional Tax on Early Distributions from Qualified Retirement Plans**

- 72(t)(1): Imposition of Additional Tax: Increases by 10%
- 72(t)(2)(A)(i): Subsection not to Apply to Certain Distributions: The increase of 10% does not apply for distributions which are made on or after the date on which the ee attains age 59½.
- 72(t)(2)(A)(iv): The 10% increase does not apply to part of a series of equal periodical payments (not less frequently than annually) made for the life of the ee or the joint lives of such ee and his designated beneficiary.
- 72(t)(2)(E): Distributions from Individual Retirement Plans for Higher Education Expenses: if the distribution do not exceed the qualified higher education expenses, then the distribution is not taxed an additional 10%.
- 72(t)(2)(F): Distributions from Certain Plans for First Home Purchasers: if the distribution is for a qualified first-time homebuyer then the 10% does not apply.

**72(a)-(b)(2), (c)(1), (e)(1)-(3), (q)(1) – Annuities**

72(a): General Rule for Annuities: Gross income includes any amount received as an annuity

72(b): Exclusion Ratio: (1) Gross income does not include the part of the amount received as an annuity which bears the same ratio to such amount as the investment in the contract to the expected return under the contract. (2) The amount excluded under 1 shall not exceed the unrecovered investment in the contract immediately before the receipt of such amount.

72(c)(1): Definitions; Investment in the contract: The investment in the contract at the time of the annuity starting date is (A) the aggregate amount of premiums or other consideration paid for the contract, MINUS (B) the aggregate amount received under the contract before such date, to the extent that the amount was excludable from gross income.

72(e): Amounts not received as annuities:

- (1) this applies to amounts received under annuities, endowments, life insurance and any amount which is not received as an annuity if no other provision here applies to the amount,
- (2) General Rule: Any amount (A) if received on or after the annuity starting date is included in gross income, or (B) if received before the starting date (i) shall be

included in gross income to the extent allocable to income on the contract AND (ii) shall not be included in gross income to the extent allocable to the investment in the contract.

- (3) Allocation of Amounts to Income and Investment: For (2)(B),
  - (A): Any amount to which this section applies shall be treated as *allocable to income* on the contract to the extent that such amount does not exceed the excess of (i) cash value of the contract, without regard to any surrender charge, immediately before the payment is received, OVER (ii) the investment in the contract.
  - (B): Any amount to which the subsection applies shall be treated as *allocable to investment* in the contract to the extent that such amount is not allocated to income under subsection (A).

72(q)(1): 10% Penalty for premature distributions from annuity contracts; Imposition of Penalty: The penalty occurs during the taxable year in which such a payment is received for that payment that is included in gross income.

108(a)(1), (b)(1), (c), (d)(1)-(3), (e)(5), (f), 1017(a)

**108(a)(1): Income from Discharge of Indebtedness: Exclusion from Gross Income:**

- Gross income does not include any amount which would be includible in gross income of TP if:
  - (A): Discharge occurs in Bankruptcy case
  - (B): Occurs when TP is insolvent
  - (C): The indebtedness discharged is qualified farm indebtedness
  - (D): TP other than a C corporation, the indebtedness discharged is qualified real property business indebtedness.

**108(b)(1): Reduction of Tax Attributes: In General:**

- The amount excluded from gross income under (a)(1) shall be applied to reduce the tax attributes of the taxpayer in the cases of A-C.

**108(c): Treatment of Discharged of Qualified Real Property Business Indebtedness:**

- (1)(A): The amount excluded here is applied to reduce the basis of the depreciable real property of TP.
- Limitations: (2)(A): Indebtedness in Excess of Value: The amount excluded shall not exceed (i) outstanding Principle amount of the indebtedness over (ii) the FMV of the property reduced by the outstanding principle amount of any other real property indebtedness secured by this property.
  - (2)(B): Overall Limitation: The amount excluded shall not exceed the aggregate adjusted basis of depreciable real property held by TP immediately before the discharge.
- (3) – Qualified Real Property Business Indebtedness: This means:
  - (A): that which was incurred by TP in connection with real property used in a trade/business and is secured by such real property.
  - (B): Incurred before 1/1/93, or if after it is qualified acquisition indebtedness **AND**

- (C): If TP chooses to have this apply, it does not include qualified farm indebtedness. But B includes that which results from refinancing but only if it does not exceed the amount of the indebtedness being refinanced.
- (4) – Qualified Acquisition Indebtedness:
  - This means indebtedness incurred or assumed to acquire, construct, reconstruct or substantially improve such property.

**108(d)(1): Indebtedness of TP:**

- Any indebtedness (A) for which TP is liable or (B) subject to which the TP hold property.

**108(d)(2): Title 11 Case:**

- Case under Title 11 relating to bankruptcy but only if TP is under the jurisdiction of the court and the discharge is granted by the court or pursuant to a plan approved by the court.

**108(d)(3): Insolvent:**

- Excess of liabilities over the FMV value of assets. Regardless of insolvency, the amount that TP is insolvent is determined on the basis of assets and liabilities immediately before discharge.

**108(e)(5): Purchase-Money Debt Reduction for Solvent Debtor Treated as Price Reduction:**

- This happens if (A): Debt to seller of property which arose out of the purchase is reduced, (B) the reduction does not occur because of Title 11, or when the purchaser is insolvent AND (C): without this provision the reduction would be treated as income to the purchaser because of the discharge of indebtedness.

**108(f): Student Loans:**

- (1) Gross income does not include any student loan if the discharge was pursuant to a provision that provided the loan would be partially or entirely discharged if the debtor worked for a certain period of time in certain professions.
- (2): A student loan means a loan to assist the individual in attending an educational organization made by (A) US, (B) State, (C) Public benefit organization, (D) Educational Organization unless the discharge is on account of services performed for the organization.

**1017(a) Discharge of Indebtedness:**

- If an amount is excluded from gross income under 108(a) and under 108(b)(2)(E) or (b)(5) or (c)(1), any portion of such amount is to be applied to reduce basis, then the portion shall be applied in reduction of the basis of property held by the TP at the beginning of the taxable year following the taxable year in which the discharged occurred.

**104(a)(2)-(3)**

104(a)(2): The amount of any damages (other than punitive damages) received (by suit or agreement, and lump or periodic payment) on account of personal physical injuries or physical sickness is not included in gross income.

104(a)(3): Amounts received through accident or health insurance for personal injuries or sickness are not included as long as the amounts are attributable to contributions by Er which were not includible in the income of ee, or paid by Er.

### **103 – Interest on state and local Bonds**

(a): gross income does not include any interest on state and local bonds.

(b): Exceptions:

- (1): Private activity bond that is not qualified
- (2): Arbitrage Bond
- (3) Bond not in registered form
- (c): Definitions: (1) state or local bond: obligation of the state or political subdivision; (2) state – duh.

### **86(a)-(D)(1) – Social Security and Tier 1 Railroad Retirement Benefits**

(a)(1): Gross income is included social security benefits. Whichever is less is included in GI:

- (A): One-half of the SS benefits received during the year **OR**
- (B) One-half of the excess in (b)(1) – [adjusted gross income plus one-half of SS benefits exceeds the base amount].

(a)(2): **Additional Amount:** If (b)(1)(A) [the adjusted GI plus one-half of SS benefits] exceeds the adjusted base amount, the amount included in GI is equal to the lesser of:

- (A) The sum of (i) 85% of the excess, PLUS (ii) the less amount of (a)(1) or an amount equal to one-half of the difference between the adjusted base amount and the base amount of the TP **OR**
- (B): 85% of the SS Benefits received during the taxable year.

(b)(1)(A): A TP is subject in this section if the sum of (i) the modified adjusted GI PLUS (ii) one-half of the SS benefits received EXCEEDS (B) the base amount.

(b)(2): **Modified GI** means adjusted GI (A) without regard to particular sections and (B) increased by the amount of interest received or accrued by TP during the tax year which IS exempt from tax.

(c)(1): Base amount means (A) except as otherwise provided, 25K, (B) 32K in the case of a joint return, (C) Zero in the case of TP who (i) is married but does not joint file, AND (ii) does not live apart from his spouse at all times during the year.

(c)(2): Adjusted Base Amount means, (A) except otherwise, 34K, (B) 44K for joint return, (C) zero for the same reasons in (c)(1)(C).

(d)(1): SS benefit means any amount received by TP by reason of entitlement under SS act or tier 1 railroad thing.

### **B. Realization When Property Transferred as Compensation: 83(a)-(c), (h); Reg. 1.83-4(b)**

Property transferred in connection with Performance of Services

- (a): Property transferred must be in connection with services. The transfer must be to any person other than the person for whom such services are performed.
  - Then the person who performs the services must include in GI the excess of
    - (1) FMV of the property when the interest holder of the property has transferable rights or is not subject to a substantial risk of forfeiture, whatever ends earlier, OVER
    - (2) Amount paid for such property.
    - So FMV – Amount Paid.

- This does not apply to someone if TP sells or otherwise disposed of property in arm's length transaction before the rights are transferable or not subject to substantial risk of forfeiture.
- (b): Election to include in GI in year of transfer.
  - If perform service in connection with which property is transferred, TP can include in GI the transfer. This is the EXCESS of
    - FMV without regard to restrictions OVER amount paid.
  - If this is done, (a) does not apply and if the property is forfeited later then no deduction shall be allowed for loss because of forfeiture.
  - This election shall not be made less than 30 days after the transfer.
- (c): Special Rules:
  - Substantial risk of forfeiture: this means that a person's rights to full enjoyment are conditioned upon the future performance of substantial services by any individual.
  - Transferability or Property: This is the case only when TP's rights in the property are not conditioned by a substantial risk of forfeiture.

#### **1041(a)-(c) – Transfers between Spouses or Incident to Divorce**

- (a) – no gain/loss recognized if property is transferred from individual to spouse or incident to divorce.
- (b) – Transfer treated as a gift and the transferee has the transferor's basis
- (c) – incident to divorce means that it is within 1 year after the date on which the marriage ends OR is related to the marriage.

#### **1031(a)(1)-(2), (b), (d) – Exchange of Property held for productive use or investment**

- (a) Non-Recognition of Gain or Loss from Exchanges Solely in Kind
  - No gain or loss in GI if property held for productive use in a trade or business or investment is exchanged solely for property of like kind which is held either for productive use in a trade, business, or for investment.
  - There are exceptions:
    - Stock in trade or property primarily for sale, stocks/bonds, other securities, interests in P-ship, certificates of trust, choses in action.
- (b) – Gain from Exchanges not Solely in Kind
  - If non-like property or money is given, then the gain to the *recipient* shall be recognized. The gain is not in excess of the sum of the money and the FMV of the other property.
- (d) – Basis:
  - If a like exchange then the basis is the same as the property exchanged – money received + amount of gain or – the amount of loss to TP that was recognized on the exchange.

#### **1033**

- (a): If property as result of destruction, seizure, theft, requisition or condemnation or threat of is compulsory or involuntarily converted then (1) there is no gain for the conversion into similar property or (2) but there is a gain if converted into

money or into property that is not similar or related in service or use. Number 2 is qualified:

- (A): However if the money is used to replace the property with property that is similar in service or use, or purchases stock in the company that owns such similar property, then this election only results in a realized gain if the amount realized exceeds the cost of the other property or stock.
  - Exceptions: No property/stock acquired before disposition of converted property is considered to have been acquired for replacement unless held by TP on the date of disposition. TP shall be considered to have purchased property only if the unadjusted basis of such stock would be its cost within the meaning of 1012.
- (B): Period within which property must be replaced: The time starts at the date of disposition of converted property or the earliest date of the threat or imminence of reacquisition or condemnation of the converted property. This goes for 2 years after the close of the first taxable year or is subject to the terms and conditions of the secretary.
- (b): Basis for property acquired through involuntary conversion:
  - (1) FOR (a)(1): The basis is the same as in the case of the converted property AND
    - Offset by any amount received that was not used for replacement property AND
    - Increased in the amount of gain or decreased in the amount of loss to TP recognized upon the conversion when it was made.
  - (2) FOR (a)(2): If some of the gain was non-recognized, then the basis is the cost of the property decreased in the amount of the gain that was not recognized. If there are more than 1 property in the deal, then the cost is allocated in proportion to respective costs.
  - (3): Property held by Corporation the stock of which is replacement property.
    - (A): If the basis is decreased, then the amount equal to the decrease is applied to reduce the basis held by the company at the time TP acquired control.
    - (B): Limitation: (A) does not apply if it would reduce the aggregate bases of the property of the company below TP's adjusted basis of the stock in the company.
    - (C): Allocation of Basis Reduction: The decrease under (A) is allocated (i) first to property which is similar or related in service or use, (ii) then to depreciable property, (iii) then to other property.
    - (D): The reduction shall not exceed the adjusted basis of the property.
    - If more than 1 property is under C, the reduction is allocated in proportion to the adjusted basis of such property.