



Instructions for Schedule D (Form 1120S)

Capital Gains and Losses and Built-in Gains

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

Future Developments

For the latest information about developments related to Schedule D (Form 1120S) and its instructions, such as legislation enacted after they were published, go to www.irs.gov/form1120s.

What's New

Form 8949. Many transactions that, in previous years, would have been reported on Schedule D must be reported on Form 8949, Sales and Other Dispositions of Capital Assets. For 2012, Schedule D (Form 1120S) filers will not list separate capital asset transactions on Schedule D (Form 1120S). Instead, Schedule D (Form 1120S) filers that have transactions that must be listed on line 1, 2, 3, 8, 9, or 10 must complete Form 8949 before completing line 1, 2, 3, 8, 9, or 10. See the instructions for Form 8949.

Built-in gains. For tax years beginning in 2012 or 2013, the recognition period for built-in gains tax is a 5-year period. See [Part III. Built-in Gains Tax](#) and section 1374(d)(7).

In addition, for tax years beginning after 2011, the treatment of all payments received from an installment sale follows certain built-in gains tax rules in effect for the tax year of the sale. See section 1374(d)(7)(E).

General Instructions

Purpose of Schedule

Use Schedule D to report the following.

- The overall capital gains and losses from transactions listed on Form 8949.
- Gains on distributions to shareholders of appreciated capital assets.
- Capital gain from Form 6252, Installment Sale Income.
- Capital gain or loss from Form 8824, Like-Kind Exchanges.
- Tax on built-in gains. See [Part III. Built-in Gains Tax](#).

Other Forms the Corporation May Have To File

Use Form 4797, Sales of Business Property, to report the following.

- The sale, exchange, or distribution of property used in a trade or business.
- The sale, exchange, or distribution of depreciable and amortizable property.
- The sale or other disposition of securities or commodities held in connection with a trading business, if the corporation made a mark-to-market election.
- The involuntary conversion (from other than casualty or theft) of property used in the corporation's trade or business and capital assets held in connection with a trade or business or a transaction entered into for profit.
- The disposition of noncapital assets other than inventory or property held primarily for sale to customers in the ordinary course of the corporation's trade or business.

Use Form 4684, Casualties and Thefts, to report involuntary conversions of property due to casualty or theft.

Use Form 6781, Gains and Losses From Section 1256 Contracts and Straddles, to report gains and losses from section 1256 contracts and straddles.

Additional information. For more information, see Pub. 544, Sales and Other Dispositions of Assets, and Pub. 550, Investment Income and Expenses (Including Capital Gains and Losses).

Capital Assets

Each item of property the corporation held (whether or not connected with its trade or business) is a capital asset except the following. See section 1221(a).

- Stock in trade or other property included in inventory or held mainly for sale to customers. However, see the *Note* below.
- 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 included in inventory or held mainly for sale to customers.
- Depreciable or real property used in the trade or business, even if it is fully depreciated.

- Certain copyrights; literary, musical, or artistic compositions; letters or memoranda; or similar property. However, see the *Note* below.
- U.S. Government publications, including the Congressional Record, that the corporation received from the Government, other than by purchase at the normal sales price, or that the corporation got from another taxpayer who had received it in a similar way, if the corporation's basis is determined by reference to the previous owner's basis.
- Certain commodities derivative financial instruments held by a dealer not in connection with its dealer activities.
- Certain identified hedging transactions entered into in the normal course of the trade or business.
- Supplies regularly used in the trade or business.

Note. The corporation can elect to treat as capital assets certain musical compositions or copyrights it sold or exchanged. See section 1221(b)(3) and Pub. 550 for details.

Items for Special Treatment

Note. For more information, see Pub. 544.

Loss from a sale or exchange between the corporation and a related person. Except for distributions in complete liquidation of a corporation, no loss is allowed from the sale or exchange of property between the corporation and certain related persons. See section 267.

Loss from a wash sale. The corporation cannot deduct a loss from a wash sale of stock or securities (including contracts or options to acquire or sell stock or securities) unless the corporation is a dealer in stock or securities and the loss was sustained in a transaction made in the ordinary course of the corporation's trade or business. A wash sale occurs if the corporation acquires (by purchase or exchange), or has a contract or option to acquire, substantially identical stock or securities within 30 days before or after the date of the sale or exchange. See section 1091.

Report a wash sale transaction on Form 8949, Part I or Part II (with the appropriate box checked). Enter "W" in

column (f) and enter as a positive number in column (g) the amount of the loss not allowed. Complete all remaining columns. See the Instructions for Form 8949.

Gain on distributions of appreciated property. Generally, gain (but not loss) is recognized on a nonliquidating distribution of appreciated property to the extent that the property's fair market value exceeds its adjusted basis. See section 311.

Gain or loss on distribution of property in complete liquidation. Generally, gain or loss is recognized on property distributed in a complete liquidation. Treat the property as if it had been sold at its fair market value. See section 336.

Gain or loss on certain short-term federal, state, and municipal obligations (other than tax-exempt obligations). These obligations are treated as capital assets in determining gain or loss. On any gain realized, a portion is treated as ordinary income and any remaining balance as a short-term capital gain. See section 1271(a)(3).

Gain from installment sales. If the corporation sold property at a gain and it will receive a payment in a tax year after the year of sale, it generally must report the sale on the installment method unless it elects not to. However, the installment method may not be used to report sales of stock or securities traded on an established securities market.

Use Form 6252 to report the sale on the installment method. Also use Form 6252 to report any payment received during the tax year from a sale made in an earlier year that was reported on the installment method.

To elect out of the installment method, report the full amount of the gain on Form 8949 for the year of the sale on a return filed by the due date (including extensions). If the original return was filed on time without making the election, the corporation can make the election on an amended return filed no later than 6 months after the original due date (excluding extensions). Write "Filed pursuant to section 301.9100-2" at the top of the amended return.

Gain or loss on an option to buy or sell property. See sections 1032 and 1234 for the rules that apply to a purchaser or grantor of an option or a securities futures contract (as defined in section 1234B). See Pub. 550 for details.

Gain or loss from a short sale of property. Report the gain or loss to the extent that the property used to close the short sale is considered a capital asset in the hands of the taxpayer.

Loss from securities that are capital assets that become worthless during the year. Except for securities held by a

bank, treat the loss as a capital loss as of the last day of the tax year. See section 582 for the rules on the treatment of securities held by a bank.

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 corporation can elect not to recognize gain from the sale of certain stock to an ESOP or an eligible cooperative.

Bonds and other debt instruments. See Pub. 550.

Nonbusiness bad debts. A nonbusiness bad debt must be treated as a short-term capital loss and can be deducted only in the year the debt becomes totally worthless. See *Nonbusiness Bad Debts* in Pub. 550 for details.

Real estate subdivided for sale. Certain lots or parcels that are part of a tract of real estate subdivided for sale may be treated as capital assets. See section 1237.

Sale of a partnership interest. A sale or other disposition of an interest in a partnership owning unrealized receivables or inventory items may result in ordinary gain or loss. See Pub. 541, Partnerships.

Special rules for traders in securities. Traders in securities are engaged in the business of buying and selling securities for their own account. To be engaged in a business as a trader in securities, the corporation:

- Must seek to profit from daily market movements in the prices of securities and not from dividends, interest, or capital appreciation.
- Must be involved in a trading activity that is substantial.
- Must carry on the activity with continuity and regularity.

The following facts and circumstances should be considered in determining if a corporation's activity is a business.

- Typical holding periods for securities bought and sold.
- The frequency and dollar amount of the corporation's trades during the year.
- The extent to which the shareholders pursue the activity to produce income for a livelihood.
- The amount of time devoted to the activity.

Like an investor, a trader must report each sale of securities (taking into account commissions and any other costs of acquiring or disposing of the securities) on Form 8949 or on an attached statement containing all the same information for each sale in a similar format. However, if a trader made the mark-to-market election

(see the Instructions for Form 4797), each transaction is reported in Part II of Form 4797 instead of on Form 8949.

The limitation on investment interest expense that applies to investors does not apply to interest paid or incurred in a trading business. A trader reports interest expense and other expenses (excluding commissions and other costs of acquiring and disposing of securities) from a trading business on page 1 of Form 1120S.

A trader also may hold securities for investment. The rules for investors generally will apply to those securities. If they apply, allocate interest and other expenses between your trading business and investment securities. Report investment interest expense on line 12b of Schedule K and in box 12 of Schedule K-1 using code H.

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

Gain on the constructive sale of certain appreciated financial positions. Generally, if the corporation holds an appreciated financial position in stock or certain other interests, it may have to recognize gain (but not loss) if it enters into a constructive sale (such as a "short sale against the box"). See Pub. 550.

Rollover of gain from qualified stock. If the corporation sold qualified small business (QSB) stock (defined below) it held for more than 6 months, it can postpone gain if it purchased other QSB stock during the 60-day period that began on the date of the sale. The corporation 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 corporation chooses to postpone gain, report the entire gain realized on the sale on Form 8949, Part I or Part II (with the appropriate box checked). Enter "R" in column (f) and enter the amount of the postponed gain as a negative number (in parentheses) in column (g). Complete all remaining columns. See the Instructions for Form 8949.



The corporation also must separately state the amount of the gain rolled over on qualified stock under section 1045 on Form 1120S, Schedule K, line 10, because each shareholder must determine if he or she qualifies for the rollover at the shareholder level. Also, the corporation must separately state on that line (and not on Form 8949) any gain that could qualify for the section 1045 rollover at the

shareholder level instead of the corporate level (because a shareholder was entitled to purchase replacement stock). If the corporation had a gain on qualified stock that could qualify for the exclusion under section 1202, report that gain on Form 8949 (and on Form 1120S, Schedule K, line 10).

To be QSB stock, the stock must meet all of the following tests.

- It must be stock in a C corporation.
- 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 corporation must have acquired the stock at its original issue (either directly or through an underwriter), either in exchange for money or other property or as pay for services (other than as an underwriter) to the corporation. In certain cases, the corporation may meet the test if it acquired the stock from another person who met this test (such as by gift or inheritance) or through a conversion or exchange of qualified small business stock held by the corporation.
- During substantially all the time the corporation held the stock:
 1. The issuer was a C corporation,
 2. At least 80% of the value of the issuer's assets were used in the active conduct of one or more qualified businesses (defined below), and
 3. The issuing corporation was not a foreign corporation, DISC, former DISC, corporation that has made (or that has a subsidiary that has made) a section 936 election, regulated investment company, real estate investment trust, REMIC, 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.

For more details about limits and additional requirements that may apply, see Pub. 550 or section 1202.

Exclusion of gain from DC Zone assets. If the corporation sold or exchanged a District of Columbia Enterprise Zone (DC Zone) asset acquired after 1997 and before 2012, and held for more than 5 years, it can exclude any qualified capital gain. The sale or exchange of DC Zone capital assets reported on Schedule D include:

- 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 corporation'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 attributable to unrecaptured section 1250 gain on the sale of an interest in a partnership that is a DC Zone business. See the instructions for line 8c of Schedule K for information on how to report unrecaptured section 1250 gain.
- Gain on the sale of an interest in a partnership attributable to real property or an intangible asset that is not an integral part of a DC Zone business.
- Gain from a related-party transaction. See *Sales and Exchanges Between Related Persons* in chapter 2 of Pub. 544.

See section 1400B for more details on DC Zone assets and special rules.

How to report. Report the sale or exchange as the corporation otherwise would without regard to the exclusion on Form 8949, Part II (with the appropriate box checked). Enter "X" in column (f) and enter the amount of the exclusion as a negative number (in parentheses) in column (g). Complete all remaining columns. See the Instructions for Form 8949 for details.

Exclusion of gain from qualified community assets. If the corporation sold or exchanged a qualified community asset acquired after 2001 and before 2010, and held for more than 5 years, it may be able to exclude any qualified capital gain. The exclusion applies to an interest in, or property of, certain renewal community businesses.

Qualified community asset. A qualified community asset is any of the following.

- Qualified community stock.
- Qualified community partnership interest.
- Qualified community business property.

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 renewal community business.
- Gain from a related-party transaction. See *Sales and Exchanges Between Related Persons* in chapter 2 of Pub. 544.

See section 1400F for more details on qualified community assets and special rules.

How to report. Report the sale or exchange as the corporation otherwise would without regard to the exclusion on Form 8949, Part II (with the appropriate box checked). Enter "X" in column (f) and enter the amount of the exclusion as a negative number (in parentheses) in column (g). Complete all remaining columns. See the Instructions for Form 8949.

Collectibles (28%) rate gain or (loss). Report any 28% gain or loss on line 8b of Schedule K (and each shareholder's share in box 8b of Schedule K-1). A collectibles gain or loss is any long-term gain or deductible long-term loss from the sale or exchange of a collectible that is a capital asset.

Collectibles include works of art, rugs, antiques, metals (such as gold, silver, and platinum bullion), gems, stamps, coins, alcoholic beverages, and certain other tangible property.

Report any 28% gain or loss from a sale or exchange of a collectible on Form 8949, Part II (with the appropriate box checked). See the Instructions for Form 8949.

Also include gain (but not loss) from the sale or exchange of an interest in a partnership or trust held more than 1 year and attributable to unrealized appreciation of collectibles. See Regulations section 1.1(h)-1. Also, attach the statement required under Regulations section 1.1(h)-1(e).

Specific Instructions

Complete all necessary pages of Form 8949 before you complete line 1, 2, 3, 8, 9, or 10 of Schedule D.

Rounding off to whole dollars. You can round off cents to whole dollars on your Schedule D. If you do round to whole dollars, you must round all amounts. To round, drop amounts under 50 cents and increase amounts from 50 and 99 cents to the next dollar. For example, \$1.39 becomes \$1 and \$2.50 becomes \$3.

If you have to add two or more amounts to figure the amount to enter on a line, include cents when adding the amounts and round off only the total.

Parts I and II

Lines 1, 2, 3, 8, 9, and 10, Column (h)—Gain or Loss

Figure gain or loss on each line. First, subtract cost or other basis in column (e) from proceeds (sales price) in column (d). Then combine the results with any adjustments in column (g). Enter the results in column (h). Enter negative amounts in parentheses.

Example 1—gain. Column (d) is \$6,000 and column (e) is \$2,000. Enter \$4,000 in column (h).

Example 2—loss. Column (d) is \$6,000 and column (e) is \$8,000. Enter (\$2,000) in column (h).

Example 3—adjustment. Column (d) is \$6,000, column (e) is \$2,000, and column (g) is (\$1,000). Enter \$3,000 in column (h).

Part III. Built-in Gains Tax

Section 1374 provides for a tax on built-in gains. The built-in gains tax may apply to the following S corporations.

1. An S corporation that was a C corporation before it elected to be an S corporation.
2. An S corporation that acquired an asset with a basis determined (in whole or in part) by reference to its basis (or the basis of any other property) in the hands of a C corporation (a **transferred-basis acquisition**). See section 1374(d)(8).

An S corporation may owe the tax if it has net recognized built-in gain during the applicable recognition period. For tax years beginning in 2012 or 2013, the applicable recognition period is the 5-year period beginning:

- For an asset held when the S corporation was a C corporation, on the first day of the first tax year for which the corporation is an S corporation; or
- For an asset with a basis determined by reference to its basis (or the basis of any

other property) in the hands of a C corporation, on the date the asset was acquired by the S corporation.

A corporation described in both (1) and (2), above, must figure the built-in gains tax separately for the group of assets it held at the time its S election became effective and for each group of assets it acquired from a C corporation with basis determined (in whole or in part) by reference to the basis of the asset (or any other property) in the hands of the C corporation. For details, see Regulations section 1.1374-8.

Certain transactions involving the disposal of timber, coal, or domestic iron ore under section 631 are not subject to the built-in gains tax. See Rev. Rul. 2001-50, which is on page 343 of Internal Revenue Bulletin 2001-43 at www.irs.gov/pub/irs-irbs/irb01-43.pdf.

Line 16

Generally, enter the amount that would be the taxable income of the corporation for the tax year if only recognized built-in gains (including any carryover of gain under section 1374(d)(2)(B)) and recognized built-in losses were taken into account.

Generally, recognized built-in gain includes the following items.

1. Any gain recognized during the applicable recognition period on the sale or distribution (disposition) of any asset, except to the extent the corporation establishes that:
 - a. The asset was not held by the corporation as of the beginning of the applicable recognition period, or
 - b. The gain exceeds the excess of the fair market value of the asset as of the beginning of the applicable recognition period over the adjusted basis of the asset at that time; and
2. Any item of income that is properly taken into account during the applicable recognition period but is attributable to periods before the applicable recognition period.

Generally, recognized built-in loss includes the following items.

1. Any loss recognized during the applicable recognition period on the disposition of any asset to the extent the corporation establishes that:
 - a. The asset was held by the corporation as of the beginning of the applicable recognition period, and
 - b. The loss does not exceed the excess of the adjusted basis of the asset as of the beginning of the applicable recognition period, over the fair market value of the asset as of that time; and
2. Any amount that is allowed as a deduction during the applicable

recognition period (determined without regard to any carryover) but is attributable to periods before the applicable recognition period.

For details, see section 1374(d) and Regulations section 1.1374-4.

The corporation must show on an attachment its total net recognized built-in gain and list separately any capital gain or loss and ordinary gain or loss.

Line 17

Figure taxable income by completing lines 1 through 28 of Form 1120. Follow the instructions for Form 1120. Enter the amount from line 28 of Form 1120 on line 17 of Schedule D. Attach to Schedule D the Form 1120 computation or other worksheet used to figure taxable income.

For corporations figuring the built-in gains tax for separate groups of assets, taxable income must be apportioned to each group of assets in proportion to the net recognized built-in gain for each group of assets. For details, see Regulations section 1.1374-8.

Note. Taxable income is figured as provided in section 1375(b)(1)(B) and is generally figured in the same manner as taxable income for line 9 of the Excess Net Passive Income Tax Worksheet for Line 22a in the Instructions for Form 1120S.

Line 18

If, for any tax year in the recognition period, the amount on line 16 exceeds the taxable income on line 17, the excess is treated as a recognized built-in gain in the succeeding tax year. This carryover provision applies only in the case of an S corporation that made its election to be an S corporation after March 30, 1988. See section 1374(d)(2)(B).

For corporations figuring the built-in gains tax for separate groups of assets, do not use the amount from Schedule B, line 8. Instead, figure the amount of net unrealized built-in gain separately for each group of assets.

Line 19

Enter the section 1374(b)(2) deduction. Generally, this is any net operating loss carryforward or capital loss carryforward (to the extent of net capital gain included in recognized built-in gain for the tax year) either arising in tax years for which the corporation was a C corporation or acquired in a transferred-basis acquisition (defined earlier). The section 1374(b)(2) deduction must be figured and applied separately for each separate group of assets. See section 1374(b)(2) and Regulations section 1.1374-5.

Line 22

Enter the section 1374(b)(3) credit. Generally, this is any general business credit arising in tax years for which the corporation was a C corporation or acquired in a transferred-basis acquisition (defined earlier). The section 1374(b)(3) credit must be figured and applied separately for each separate group of assets. Section 1374(b)(3) business credit and minimum tax credit carryforwards from C corporation years are subject to the business credit limitation in section 38(c) and the AMT credit limitation in section 53(c), as modified by Regulations section 1.1374-6(b).

If corporations made the section 168(k) (4) election in prior years, they can elect to increase these limitations for pre-2006 unused minimum tax credits in lieu of claiming the special depreciation

allowance for certain property acquired after March 31, 2008, and placed in service before January 1, 2013. (For corporations with tax years ending after December 31, 2012, this election is available for certain property placed in service before January 1, 2014.) For details, see Form 4562, Depreciation and Amortization; Form 8827, Credit for Prior Year Minimum Tax—Corporations; and related instructions. Also, see Rev. Proc. 2009-33, 2009-29 I.R.B. 150, available at www.irs.gov/irb/2009-29_IRB/ar09.html; Rev. Proc. 2009-16, 2009-6 I.R.B. 449, available at www.irs.gov/irb/2009-06_IRB/ar10.html; and Rev. Proc. 2008-65, 2008-44 I.R.B. 1082, available at www.irs.gov/irb/2008-44_IRB/ar15.html.



An S corporation that made this election can use the credit carryforwards only against the built-in gains tax. The refundable credit provisions do not apply to S corporations.

Line 23

The built-in gains tax is treated as a loss sustained by the corporation during the same tax year. The character of the deemed loss is determined by allocating the loss proportionately among the net recognized built-in gains giving rise to the tax and attributing the character of each net recognized built-in gain to the allocable portion of the loss. Deduct the tax attributable to:

- Short-term capital gain as short-term capital loss on Schedule D, line 6.
- Long-term capital gain as long-term capital loss on Schedule D, line 14.
- Ordinary income as a deduction for taxes on Form 1120S, line 12.