



# Instructions for Form 1041 and Schedules A, B, D, G, I, J, and K-1

## U.S. Income Tax Return for Estates and Trusts

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

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Photographs of missing children selected by the Center may appear in instructions on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1-800-THE-LOST** (1-800-843-5678) if you recognize a child.

### Unresolved Tax Issues

If you have attempted to deal with an IRS problem unsuccessfully, you should contact the Taxpayer Advocate. The Taxpayer Advocate independently represents the estate's or trust's interests and concerns within the IRS by protecting its rights and resolving problems that have not been fixed through normal channels.

While Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that the estate's or trust's case is given a complete and impartial review.

The estate's or trust's assigned personal advocate will listen to its point of view and will work with the estate or trust to address its concerns. The estate or trust can expect the advocate to provide:

- A "fresh look" at a new or on-going problem.
- Timely acknowledgment.
- The name and phone number of the individual assigned to its case.
- Updates on progress.
- Timeframes for action.
- Speedy resolution.
- Courteous service.

When contacting the Taxpayer Advocate, you should provide the following information:

- The estate's or trust's name, address, and employer identification number.
- The name and telephone number of an authorized contact person and the hours he or she can be reached.
- The type of tax return and year(s) involved.
- A detailed description of the problem.
- Previous attempts to solve the problem and the office that had been contacted.
- A description of the hardship the estate or trust is facing (if applicable).

The estate or trust may contact a Taxpayer Advocate by calling

### Changes To Note

- The tax rates of 27%, 30%, 35%, and 38.6% have been reduced to 25%, 28%, 33%, and 35%, respectively. The 10% rate for bankruptcy estates has been expanded to the first \$7,000 of taxable income. These changes are reflected in the tax rate schedules on pages 11 and 21.

- The maximum tax rate for qualified dividends is 15% (generally, 5% if the other income of the estate or trust is taxed at the 15% rate). For details on qualified dividends, see the instructions for line 2b on page 14. Use **Schedule D (Form 1041)** or the **Qualified Dividends Tax Worksheet** on page 22, whichever applies, to figure the tax.

- For tax years beginning in 2003, the requirement to file a return for a bankruptcy estate applies only if gross income is at least \$7,800.

- For 2003, qualified disability trusts can claim an exemption of up to \$3,050. See the instructions for line 20 on page 18 for more details.

### Photographs of Missing Children

The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children.

**1-877-777-4778** (toll free). Persons who have access to TTY/TDD equipment may call 1-800-829-4059 and ask for Taxpayer Advocate assistance. If the estate or trust prefers, it may call, write, or fax the Taxpayer Advocate office in its area. See **Pub. 1546**, The Taxpayer Advocate Service of the IRS, for a list of addresses and fax numbers.

## How To Get Forms and Publications

### Personal Computer

You can access the IRS web site 24 hours a day, 7 days a week at **www.irs.gov** to:

- Download forms, instructions, and publications.
- Order IRS products online.
- See answers to frequently asked tax questions.
- Search publications online by topic or keyword.
- Send us comments or request help by email.
- Sign up to receive local and national tax news by email.

You can also reach us using file transfer protocol at **ftp.irs.gov**.

### CD-ROM

Order **Pub. 1796**, Federal Tax Products on CD-ROM, and get:

- Current year forms, instructions, and publications.
- Prior year forms, instructions, and publications.
- Frequently requested tax forms that may be filled in electronically, printed out for submission, and saved for recordkeeping.
- The Internal Revenue Bulletin.

Buy the CD-ROM on the Internet at **www.irs.gov/cdorders** from the National Technical Information Service (NTIS) for \$22 (no handling fee) or call **1-877-CDFORMS** (1-877-233-6767) toll free to buy the CD-ROM for \$22 (plus a \$5 handling fee).

### By Phone and in Person

You can order forms and publications 24 hours a day, 7 days a week, by calling **1-800-TAX-FORM** (1-800-829-3676). You can also get most forms and publications at your local IRS office.

## General Instructions

### Purpose of Form

The fiduciary of a domestic decedent's estate, trust, or bankruptcy estate uses Form 1041 to report:

- The income, deductions, gains, losses, etc. of the estate or trust;
- The income that is either accumulated or held for future distribution or distributed currently to the beneficiaries;
- Any income tax liability of the estate or trust; and
- Employment taxes on wages paid to household employees.

## Income Taxation of Trusts and Decedents' Estates

A trust (except a grantor type trust) or a decedent's estate is a separate legal entity for Federal tax purposes. A decedent's estate comes into existence at the time of death of an individual. A trust may be created during an individual's life (inter vivos) or at the time of his or her death under a will (testamentary). If the trust instrument contains certain provisions, then the person creating the trust (the grantor) is treated as the owner of the trust's assets. Such a trust is a grantor type trust. See page 5 for special rules for grantor trusts.

A trust or decedent's estate figures its gross income in much the same manner as an individual. Most deductions and credits allowed to individuals are also allowed to estates and trusts. However, there is one major distinction. A trust or decedent's estate is allowed an income distribution deduction for distributions to beneficiaries. To figure this deduction, the fiduciary must complete Schedule B. The income distribution deduction determines the amount of any distributions taxed to the beneficiaries.

For this reason, a trust or decedent's estate sometimes is referred to as a "pass-through" entity. The beneficiary, and not the trust or decedent's estate, pays income tax on his or her distributive share of income. Schedule K-1 (Form 1041) is used to notify the beneficiaries of the amounts to be included on their income tax returns.

Before preparing Form 1041, the fiduciary must figure the accounting income of the estate or trust under the will or trust instrument and applicable local law to determine the amount, if any, of income that is required to be distributed, because the income distribution deduction is based, in part, on that amount.

### Abusive Trust Arrangements

Certain trust arrangements purport to reduce or eliminate Federal taxes in ways that are not permitted under the law. Abusive trust arrangements typically are promoted by the promise of tax benefits with no meaningful change in the taxpayer's control over or benefit from the taxpayer's income or assets. The promised benefits may include reduction or elimination of income subject to tax; deductions for personal expenses paid by the trust; depreciation deductions of an owner's personal residence and furnishings; a stepped-up basis for property transferred to the trust; the reduction or elimination of self-employment taxes; and the reduction or elimination of gift and estate taxes. These promised benefits are inconsistent with the tax rules applicable to trust arrangements.

Abusive trust arrangements often use trusts to hide the true ownership of assets and income or to disguise the substance of transactions. These arrangements frequently involve more than one trust, each holding different assets of the taxpayer (e.g., the taxpayer's business, business equipment, home, automobile, etc.). Some trusts may hold interests in other trusts, purport to involve charities, or are foreign trusts. Funds may flow from one trust to another trust by way of rental agreements, fees for services, purchase agreements, and distributions.

Some of the abusive trust arrangements that have been identified include unincorporated business trusts (or organizations), equipment or service trusts, family residence trusts, charitable trusts, and final trusts. In each of these trusts, the original owner of the assets that are nominally subject to the trust effectively retains the authority to cause financial benefits of the trust to be directly or indirectly returned or made available to the owner. For example, the trustee may be the promoter, or a relative or friend of the owner who simply carries out the directions of the owner whether or not permitted by the terms of the trust.

When trusts are used for legitimate business, family, or estate planning purposes, either the trust, the beneficiary, or the transferor to the trust will pay the tax on income generated by the trust property. Trusts cannot be used to transform a taxpayer's personal, living, or educational expenses into deductible items, and will not seek to avoid tax liability by ignoring either the true ownership of income and assets or the true substance of transactions. Therefore, the tax results promised by the promoters of abusive trust arrangements are not allowable under the law, and the participants in and promoters of these arrangements may be subject to civil or criminal penalties in appropriate cases.

For more details, including the legal principles that control the proper tax treatment of these abusive trust arrangements, see Notice 97-24, 1997-1 C.B. 409.

## Definitions

### Beneficiary

A beneficiary includes an heir, a legatee, or a devisee.

### Distributable Net Income (DNI)

The income distribution deduction allowable to estates and trusts for amounts paid, credited, or required to be distributed to beneficiaries is limited to distributable net income (DNI). This amount, which is figured on Schedule B, line 7, is also used to determine how much of an amount paid, credited, or required to be distributed to a beneficiary will be includable in his or her gross income.

## Income, Deductions, and Credits in Respect of a Decedent

**Income.** When completing Form 1041, you must take into account any items that are income in respect of a decedent (IRD).

In general, income in respect of a decedent is income that a decedent was entitled to receive but that was not properly includible in the decedent's final income tax return under the decedent's method of accounting.

IRD includes:

- All accrued income of a decedent who reported his or her income on the cash method of accounting;
- Income accrued solely because of the decedent's death in the case of a decedent who reported his or her income on the accrual method of accounting; and
- Income to which the decedent had a contingent claim at the time of his or her death.

Some examples of IRD of a decedent who kept his or her books on the cash method are:

- Deferred salary payments that are payable to the decedent's estate.
- Uncollected interest on U.S. savings bonds.
- Proceeds from the completed sale of farm produce.
- The portion of a lump-sum distribution to the beneficiary of a decedent's IRA that equals the balance in the IRA at the time of the owner's death. This includes unrealized appreciation and income accrued to that date, less the aggregate amount of the owner's nondeductible contributions to the IRA. Such amounts are included in the beneficiary's gross income in the tax year that the distribution is received.

The IRD has the same character it would have had if the decedent lived and received such amount.

**Deductions and credits.** The following deductions and credits, when paid by the decedent's estate, are allowed on Form 1041 even though they were not allowable on the decedent's final income tax return:

- Business expenses deductible under section 162.
- Interest deductible under section 163.
- Taxes deductible under section 164.
- Investment expenses described in section 212 (in excess of 2% of AGI).
- Percentage depletion allowed under section 611.
- Foreign tax credit.

For more information, see section 691 or Income in Respect of a Decedent in **Pub. 559**, Survivors, Executors, and Administrators.

## Income Required To Be Distributed Currently

Income required to be distributed currently is income that is required under the terms of the governing instrument and

applicable local law to be distributed in the year it is received. The fiduciary must be under a duty to distribute the income currently, even if the actual distribution is not made until after the close of the trust's tax year. See Regulations section 1.651(a)-2.

## Fiduciary

A fiduciary is a trustee of a trust; or an executor, executrix, administrator, administratrix, personal representative, or person in possession of property of a decedent's estate.

**Note:** Any reference in these instructions to "you" means the fiduciary of the estate or trust.

## Trust

A trust is an arrangement created either by a will or by an inter vivos declaration by which trustees take title to property for the purpose of protecting or conserving it for the beneficiaries under the ordinary rules applied in chancery or probate courts.

## Who Must File

### Decedent's Estate

The fiduciary (or one of the joint fiduciaries) must file Form 1041 for a domestic estate that has:

1. Gross income for the tax year of \$600 or more or
2. A beneficiary who is a nonresident alien.

An estate is a **domestic estate** if it is **not** a foreign estate. A **foreign estate** is one the income of which, from sources outside the United States that is not effectively connected with the conduct of a U.S. trade or business, is not includible in gross income. If you are the fiduciary of a foreign estate, file **Form 1040NR**, U.S. Nonresident Alien Income Tax Return, instead of Form 1041.

## Trust

The fiduciary (or one of the joint fiduciaries) must file Form 1041 for a domestic trust taxable under section 641 that has:

1. Any taxable income for the tax year,
2. Gross income of \$600 or more (regardless of taxable income), or
3. A beneficiary who is a nonresident alien.

Two or more trusts are treated as one trust if such trusts have substantially the same grantor(s) and substantially the same primary beneficiary(ies) and a principal purpose of such trusts is avoidance of tax. This provision applies only to that portion of the trust that is attributable to contributions to corpus made after March 1, 1984.

A trust is a **domestic trust** if:

- A U.S. court is able to exercise primary supervision over the administration of the trust (court test) and

- One or more U.S. persons have the authority to control all substantial decisions of the trust (control test).

See Regulations section 301.7701-7 for more information on the court and control tests.

Also treated as a domestic trust is a trust (other than a trust treated as wholly owned by the grantor) that:

- Was in existence on August 20, 1996,
- Was treated as a domestic trust on August 19, 1996, and
- Elected to continue to be treated as a domestic trust.

A trust that is not a domestic trust is treated as a foreign trust. If you are the trustee of a foreign trust, file Form 1040NR instead of Form 1041. Also, a foreign trust with a U.S. owner generally must file **Form 3520-A**, Annual Information Return of Foreign Trust With a U.S. Owner.

If a domestic trust becomes a foreign trust, it is treated under section 684 as having transferred all of its assets to a foreign trust, except to the extent a grantor or another person is treated as the owner of the trust when the trust becomes a foreign trust.

## Special Rule for Certain Revocable Trusts

Section 645 provides that if both the executor (if any) of an estate (the related estate) and the trustee of a qualified revocable trust (QRT) elect the treatment in section 645, the trust shall be treated and taxed as part of the related estate during the election period. This election may be made by a QRT even if no executor is appointed for the related estate.

In general, Form 8855 must be filed by the due date for Form 1041 for the first tax year of the related estate. This applies even if the combined related estate and electing trust do not have sufficient income to be required to file Form 1041. However, if the estate is granted an extension of time to file Form 1041 for its first tax year, the due date for Form 8855 is the extended due date.

Once made, the election is irrevocable.

**Qualified revocable trusts.** In general, a QRT is any trust (or part of a trust) that, on the day the decedent died, was treated as owned by the decedent because the decedent held the power to revoke the trust as described in section 676. An electing trust is a QRT for which a section 645 election has been made.

**Election period.** The election period is the period of time during which an electing trust is treated as part of its related estate.

The election period begins on the date of the decedent's death and terminates on the earlier of:

- The day on which the electing trust and related estate, if any, distribute all of their assets or
- The day before the applicable date.

To determine the applicable date, first determine whether a **Form 706**, United States Estate (and Generation-Skipping Transfer) Tax Return, is required to be filed as a result of the decedent's death. If no Form 706 is required to be filed, the applicable date is 2 years after the date of the decedent's death. If Form 706 is required, the applicable date is the later of 2 years after the date of the decedent's death or 6 months after the final determination of liability for estate tax. For additional information, see Regulations section 1.645-1(f).

**Taxpayer identification number.** All QRTs must obtain a new taxpayer identification number (TIN) following the death of the decedent whether or not a section 645 election is made. (Use **Form W-9**, Request for Taxpayer Identification Number and Certification, to notify payers of the new TIN.)

An electing trust that continues after the termination of the election period does not need to obtain a new TIN following the termination unless:

- An executor was appointed and agreed to the election after the electing trust made a valid section 645 election, and the electing trust had filed a return as an estate under the trust's TIN or
- No executor was appointed and the QRT was the filing trust (as explained below).

A related estate that continues after the termination of the election period does not need to obtain a new TIN.

For more information about TINs, including trusts with multiple owners, see Regulations sections 1.645-1 and 301.6109-1(a).

#### **General procedures for completing Form 1041 during the election period.**

**If there is an executor.** The following rules apply to filing Form 1041 while the election is in effect:

- The executor of the related estate is responsible for filing Form 1041 for the estate and all electing trusts. The return is filed under the name and TIN of the related estate. Be sure and check the Decedent's estate box at the top of Form 1041. The executor continues to file Form 1041 during the election period even if the estate distributes all of its assets before the end of the election period.
- The Form 1041 includes all items of income, deduction, and credit for the estate and all electing trusts.
- The executor must attach a statement to Form 1041 providing the following information for each electing trust: **(a)** the name of the electing trust, **(b)** the TIN of the electing trust, and **(c)** the name and address of the trustee of the electing trust.
- The related estate and the electing trust are treated as separate shares for purposes of computing distributable net income and applying distribution provisions. Also, each of those shares can contain two or more separate shares. For more information, see **Separate**

**share rule** on page 20 and Regulations section 1.645-1(e)(2)(iii).

- The executor is responsible for insuring that the estate's share of the combined tax obligation is paid.

For additional information, including treatment of transfers between shares and charitable contribution deductions, see Regulations section 1.645-1(e).

**If there is no executor.** If no executor has been appointed for the related estate, the trustee of the electing trust files Form 1041 as if it was an estate. File using the TIN that the QRT obtained after the death of the decedent. The trustee can choose a fiscal year as the trust's tax year during the election period. Be sure to check the Decedent's estate box at the top of page 1 during the election period. The electing trust is entitled to a single \$600 personal exemption on returns filed for the election period.

If there is more than one electing trust, the trusts must appoint one trustee as the filing trustee. Form 1041 is filed under the name and TIN of the filing trustee's trust. A statement providing the same information regarding the electing trusts (except the filing trust) that is listed under **If there is an executor** above must be attached to these Forms 1041. All electing trusts must choose the same tax year.

If there is more than one electing trust, the filing trustee is responsible for insuring that the filing trust's share of the combined tax liability is paid.

For additional information on filing requirements when there is no executor, including application of the separate share rule, see Regulations section 1.645-1(e). For information on the requirements when an executor is appointed after an election is made and the executor does not agree to the election, see below.

**Responsibilities of the trustee when there is an executor (or there is no executor and the trustee is not the filing trustee).** When there is an executor (or there is no executor and the trustee is not the filing trustee), the trustee of an electing trust is responsible for the following during the election period:

- To timely provide the executor with all the trust information necessary to allow the executor to file a complete, accurate, and timely Form 1041.
- To insure that the electing trust's share of the combined tax liability is paid.

The trustee does not file a Form 1041 during the election period (except for a final return if the trust terminates during the election period as explained below).

#### **Procedures for completing Form 1041 for the year in which the election terminates.**

**If there is an executor.** If there is an executor, the Form 1041 filed under the name and TIN of the related estate for the tax year in which the election terminates

includes **(a)** the items of income, deduction, and credit for the related estate for its entire tax year, and **(b)** the income, deductions, and credits for the electing trust for the period that ends with the last day of the election period. If the estate will not continue after the close of the tax year, indicate that this Form 1041 is a final return.

At the end of the last day of the election period, the combined entity is deemed to distribute the share comprising the electing trust to a new trust. All items of income, including net capital gains, that are attributable to the share comprising the electing trust are included in the calculation of distributable net income of the electing trust and treated as distributed. The distribution rules of sections 661 and 662 apply to this *deemed distribution*. The combined entity is entitled to an income distribution deduction for this deemed distribution, and the "new" trust must include its share of the distribution in its income. See Regulations sections 1.645-1(e)(2)(iii) and 1.645-1(h) for more information.

If the electing trust continues in existence after the termination of the election period, the trustee must file Form 1041 under the name and TIN of the trust, using the calendar year as its accounting period, if it is otherwise required to file.

**If there is no executor.** If there is no executor, the following rules apply to filing Form 1041 for the tax year in which the election period ends:

- The tax year of the electing trust closes on the last day of the election period, and the Form 1041 filed for that tax year includes all items of income, deduction, and credit for the electing trust for the period beginning with the first day of the tax year and ending with the last day of the election period.
- The deemed distribution rules discussed above apply.
- Check the box to indicate that this Form 1041 is a final return.
- If the filing trust continues after the termination of the election period, the trustee must obtain a new TIN. If the trust meets the filing requirements, the trustee must file a Form 1041 under the new TIN for the period beginning with the day after the close of the election period and, in general, ending December 31 of that year.

**Responsibilities of the trustee when there is an executor (or there is no executor and the trustee is not the filing trustee).** In addition to the requirements listed above under this same heading, the trustee is responsible for the following:

- If the trust will not continue after the close of the election period, the trustee must file a Form 1041 under the name and TIN of the trust. Complete the entity information and items **A**, **C**, **D**, and **F**. Indicate in item **F** that this is a final return. Do not report any items of income, deduction, or credit.

• If the trust will continue after the close of the election period, the trustee must file a Form 1041 for the trust for the tax year beginning the day after the close of the election period and, in general, ending December 31 of that year. Use the TIN obtained after the decedent's death. Follow the general rules for completing the return.

#### Special filing instructions.

##### **When the election is not made by the due date of the QRT's Form 1041.**

If the section 645 election has not been made by the time the QRT's first income tax return would be due for the tax year beginning with the decedent's death, but the trustee and executor (if any) have decided to make a section 645 election, then the QRT is not required to file a Form 1041 for the short tax year beginning with the decedent's death and ending on December 31 of that year. However, if a valid election is not subsequently made, the QRT may be subject to penalties and interest for failure to file and failure to pay.

If the QRT files a Form 1041 for this short period, and a valid section 645 election is subsequently made, then the trustee must file an amended Form 1041 for the electing trust, excluding all items of income, deduction, and credit of the electing trust. These amounts are then included on the first Form 1041 filed by the executor for the related estate (or the filing trustee for the electing trust filing as an estate).

**Later appointed executor.** If an executor for the related estate is not appointed until after the trustee has made a valid section 645 election, the executor must agree to the trustee's election and they must file a revised Form 8855 within 90 days of the appointment of the executor. If the executor does not agree to the election, the election terminates as of the date of appointment of the executor.

If the executor agrees to the election, the trustee must amend any Form 1041 filed under the name and TIN of the electing trust for the period beginning with the decedent's death. The amended returns are still filed under the name and TIN of the electing trust, and they must include the items of income, deduction, and credit for the related estate for the periods covered by the returns. Also, attach a statement to the amended Forms 1041 identifying the name and TIN of the related estate, and the name and address of the executor. Check the Final return box on the amended return for the tax year that ends with the appointment of the executor. Except for this amended return, all returns filed for the combined entity after the appointment of the executor must be filed under the name and TIN of the related estate.

If the election terminates as the result of a later appointed executor, the executor of the related estate must file Forms 1041 under the name and TIN of

the related estate for all tax years of the related estate beginning with the decedent's death. The election period and the tax year terminate with respect to the electing trust the day before the appointment of the executor. The trustee is not required to amend any of the returns filed by the electing trust for the period prior to the appointment of the executor. The trust must file a final Form 1041 following the instructions above for completing Form 1041 in the year in which the election terminates and there is no executor.

**Termination of the trust during the election period.** If an electing trust terminates during the election period, the trustee of that trust must file a final Form 1041 by completing the entity information, checking the Final return box, and signing and dating the form. Do not report items of income, deduction, and credit. These items are reported on the related estate's return.

#### Alaska Native Settlement Trusts

The trustee of an Alaska Native Settlement Trust may elect the special tax treatment for the trust and its beneficiaries provided for in section 646. The election must be made by the due date (including extensions) for filing the trust's tax return for its first tax year ending after June 7, 2001. **Do not** use Form 1041. Use **Form 1041-N**, U.S. Income Tax Return for Electing Alaska Native Settlement Trusts, to make the election. Additionally, Form 1041-N is the trust's income tax return and satisfies the section 6039H information reporting requirement for the trust.

#### Bankruptcy Estate

The bankruptcy trustee or debtor-in-possession must file Form 1041 for the estate of an individual involved in bankruptcy proceedings under chapter 7 or 11 of title 11 of the United States Code if the estate has gross income for the tax year of \$7,800 or more. See **Of Special Interest To Bankruptcy Trustees and Debtors-in-Possession** on page 10 for details.

#### Common Trust Funds

Do not file Form 1041 for a common trust fund maintained by a bank. Instead, the fund may use **Form 1065**, U.S. Return of Partnership Income, for its return. For more details, see section 584 and Regulations section 1.6032-1.

#### Qualified Settlement Funds


The trustee of a designated or qualified settlement fund must file **Form 1120-SF**, U.S. Income Tax Return for Settlement Funds, rather than Form 1041.

## Special Filing Instructions for Grantor Type Trusts, Pooled Income Funds, and Electing Small Business Trusts

### Grantor Type Trusts

A trust is a grantor trust if the grantor retains certain powers or ownership benefits. This can also apply to only a portion of a trust. See **Grantor Type Trust** on page 12 for details on what makes a trust a grantor trust.

In general, a grantor trust is ignored for tax purposes and all of the income, deductions, etc., are treated as belonging directly to the grantor. This also applies to any portion of a trust that is treated as a grantor trust.

 **The following instructions apply only to grantor type trusts that are not using an optional filing method.**

File Form 1041 for a grantor trust unless you use an optional filing method.

If the entire trust is a grantor trust, fill in only the entity portion of Form 1041. **Do not** show any dollar amounts on the form, itself; show dollar amounts only on an attachment to the form. **Do not** use Schedule K-1 (Form 1041) as the attachment.

If only part of the trust is treated as a grantor trust, report on Form 1041 **only** the part of the income, deductions, etc., that is taxable to the trust. The amounts that are taxable directly to the grantor are shown only on an attachment to the form. **Do not** use Schedule K-1 (Form 1041) as the attachment.

On the attachment, report:

- The name, identifying number, and address of the person(s) to whom the income is taxable;
- The income of the trust that is taxable to the grantor or another person under sections 671 through 678. Report the income in the same detail as it would be reported on the grantor's return had it been received directly by the grantor; and
- Any deductions or credits that apply to this income. Report these deductions and credits in the same detail as they would be reported on the grantor's return had they been received directly by the grantor.

The income taxable to the grantor or another person under sections 671 through 678 and the deductions and credits that apply to that income **must** be reported by that person on their own income tax return.

**Example.** The John Doe Trust is a grantor type trust. During the year, the trust sold 100 shares of ABC stock for \$1,010 in which it had a basis of \$10 and 200 shares of XYZ stock for \$10 in which it had a \$1,020 basis.

The trust **does not** report these transactions on Form 1041. Instead, a schedule is attached to the Form 1041

showing each stock transaction separately and in the same detail as John Doe (grantor and owner) will need to report these transactions on his Schedule D (Form 1040). The trust may not net the capital gains and losses, nor may it issue John Doe a Schedule K-1 (Form 1041) showing a \$10 long-term capital loss.

### Optional Filing Methods for Certain Grantor Type Trusts

Generally, if a trust is treated as owned by **one** grantor or other person, the trustee may choose **Optional Method 1** or **Optional Method 2** as the trust's method of reporting instead of filing Form 1041.

Generally, if a trust is treated as owned by **two or more** grantors or other persons, the trustee may choose **Optional Method 3** as the trust's method of reporting instead of filing Form 1041.

Once you choose the trust's filing method, you must follow the rules under **Changing filing methods** if you want to change to another method.

**Exceptions.** The following trusts cannot report using the optional filing methods:

1. A common trust fund (as defined in section 584(a)).
2. A foreign trust or a trust that has any of its assets located outside the United States.
3. A qualified subchapter S trust (as defined in section 1361(d)(3)).
4. A trust all of which is treated as owned by one grantor or one other person whose tax year is other than a calendar year.
5. A trust all of which is treated as owned by one or more grantors or other persons, one of which is not a U.S. person.
6. A trust all of which is treated as owned by one or more grantors or other persons if at least one grantor or other person is an exempt recipient for information reporting purposes, unless at least one grantor or other person is not an exempt recipient and the trustee reports without treating any of the grantors or other persons as exempt recipients.

**Optional Method 1.** For a trust treated as owned by one grantor or by one other person, the trustee must give all payers of income during the tax year the name and taxpayer identification number (TIN) of the grantor or other person treated as the owner of the trust and the address of the trust. This method may be used only if the owner of the trust provides the trustee with a signed **Form W-9**, Request for Taxpayer Identification Number and Certification. In addition, unless the grantor or other person treated as owner of the trust is the trustee or a co-trustee of the trust, the trustee must give the grantor or other person treated as owner of the trust a statement that:

- Shows all items of income, deduction, and credit of the trust;
- Identifies the payer of each item of income;

- Explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and
- Informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return.



*Grantor trusts that have not applied for an EIN and are going to file under **Optional Method 1** do not need an EIN for the trust as long as they continue to report under that method.*

**Optional Method 2.** For a trust treated as owned by one grantor or by one other person, the trustee must give all payers of income during the tax year the name, address, and TIN of the trust. The trustee also must file with the IRS the appropriate Forms 1099 to report the income or gross proceeds paid to the trust during the tax year that shows the trust as the payer and the grantor or other person treated as owner as the payee. The trustee must report each type of income in the aggregate and each item of gross proceeds separately. The due date for any Forms 1099 required to be filed with the IRS by a trustee under this method is March 1, 2004 (March 31, 2004, if filed electronically).

In addition, unless the grantor or other person treated as owner of the trust is the trustee or a co-trustee of the trust, the trustee must give the grantor or other person treated as owner of the trust a statement that:

- Shows all items of income, deduction, and credit of the trust;
- Explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and
- Informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return. This statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

**Optional Method 3.** For a trust treated as owned by two or more grantors or other persons, the trustee must give all payers of income during the tax year the name, address, and TIN of the trust. The trustee also must file with the IRS the appropriate Forms 1099 to report the income or gross proceeds paid to the trust by all payers during the tax year attributable to the part of the trust treated as owned by each grantor or other person, showing the trust as the payer and each grantor or other person treated as owner of the trust as the payee. The trustee must report each type of income in the aggregate and each item of gross proceeds separately. The due date for any Forms 1099 required to be filed with

the IRS by a trustee under this method is March 1, 2004 (March 31, 2004, if filed electronically).

In addition, the trustee must give each grantor or other person treated as owner of the trust a statement that:

- Shows all items of income, deduction, and credit of the trust attributable to the part of the trust treated as owned by the grantor or other person;
- Explains how the grantor or other person treated as owner of the trust takes those items into account when figuring the grantor's or other person's taxable income or tax; and
- Informs the grantor or other person treated as the owner of the trust that those items must be included when figuring taxable income and credits on his or her income tax return. This statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

**Changing filing methods.** A trustee who previously had filed Form 1041 can change to one of the optional methods by filing a final Form 1041 for the tax year that immediately precedes the first tax year for which the trustee elects to report under one of the optional methods. On the front of the final Form 1041, the trustee must write "Pursuant to section 1.671-4(g), this is the final Form 1041 for this grantor trust," and check the "Final return" box in item F.

For more details on changing reporting methods, including changes from one optional method to another, see Regulations section 1.671-4(g).

**Backup withholding.** The following grantor trusts are treated as payors for purposes of backup withholding.

1. A trust established after 12/31/95, all of which is owned by 2 or more grantors (treating spouses filing a joint return as 1 grantor).
2. A trust with 10 or more grantors established after 12/31/83 but before 1/1/96.

For 2004, the trustee must withhold 30% of reportable payments made to any grantor who is subject to backup withholding.

For more information, see section 3406 and its regulations.

### Pooled Income Funds

If you are filing for a pooled income fund, attach a statement to support the following:

- The calculation of the yearly rate of return.
- The computation of the deduction for distributions to the beneficiaries.
- The computation of any charitable deduction.

You do not have to complete Schedules A or B of Form 1041.

If the fund has accumulations of income, file Form 1041-A unless the fund is required to distribute all of its net income to beneficiaries currently.

You must also file **Form 5227**, Split-Interest Trust Information Return, for the pooled income fund.

## Electing Small Business Trusts

Special rules apply when figuring the tax on the S portion of an electing small business trust (ESBT). The S portion of an ESBT is the portion of the trust that consists of stock in one or more S corporations and is not treated as a grantor type trust. The tax on the S portion:

- Must be figured separately from the tax on the remainder of the ESBT (if any) and attached to the return,
- Is entered to the left of the Schedule G, line 7, entry space preceded by "Sec. 641(c)," and
- Is included in the total tax on Schedule G, line 7.

The tax on the remainder (non-S portion) of the ESBT is figured in the normal manner on Form 1041.

**Tax computation attachment.** Attach to the return the tax computation for the S portion of the ESBT.

To compute the tax on the S portion:

- Treat that portion of the ESBT as if it were a separate trust.
- Include only the income, losses, deductions, and credits allocated to the ESBT as an S corporation shareholder and gain or loss from the disposition of S corporation stock.
- Aggregate items of income, losses, deductions, and credits allocated to the ESBT as an S corporation shareholder if the S portion of the ESBT has stock in more than one S corporation.
- Deduct state and local income taxes and administrative expenses directly related to the S portion or allocated to the S portion if the allocation is reasonable in light of all the circumstances.
- Do **not** claim a deduction for capital losses in excess of capital gains.
- Do **not** claim an income distribution deduction or an exemption amount.
- Do **not** deduct interest on money borrowed by the trust to buy S corporation stock.
- Do **not** use the tax rate schedule to figure the tax. The tax is **35%** of the S portion's taxable income except in figuring the maximum tax on qualified dividends and capital gains.
- Do **not** claim an exemption amount in figuring the alternative minimum tax.

For additional information, see Regulations section 1.641(c)-1.

**Other information.** When figuring the tax and DNI on the remaining (non-S) portion of the trust, disregard the S corporation items.

Do not apportion to the beneficiaries any of the S corporation items.

If the ESBT consists entirely of stock in one or more S corporations, **do not** make any entries on lines 1–22 of page 1.

Instead:

- Complete the entity portion;

- Follow the instructions above for figuring the tax on the S corporation items;

- Carry the tax from line 7 of Schedule G to line 23 on page 1; and
- Complete the rest of the return.

The grantor portion (if any) of an ESBT will follow the rules discussed under Grantor Type Trusts on page 5.

## Electronic Filing

Qualified fiduciaries or transmitters may be able to file Form 1041 and related schedules electronically. If you wish to do this, you must file **Form 9041**, Application/Registration for Electronic Filing of Business Returns. If you file Form 1041 electronically, you must also file **Form 8453-F**, U.S. Estate or Trust Income Tax Declaration and Signature for Electronic Filing. For more details, get **Pub. 1437**, Procedures and Specifications for the 1041 e-file Program U.S. Income Tax Returns for Estates and Trusts for Tax Year 2003, and **Pub. 1438**, File Specifications, Validation Criteria, and Record Layouts for the Electronic Filing Program for Form 1041, U.S. Income Tax Return for Estates and Trusts for Tax Year 2003.

## When To File

For calendar year estates and trusts, file Form 1041 and Schedules K-1 on or before April 15, 2004. For fiscal year estates and trusts, file Form 1041 by the 15th day of the 4th month following the close of the tax year. For example, an estate that has a tax year that ends on June 30, 2004, must file Form 1041 by October 15, 2004. If the due date falls on a Saturday, Sunday, or legal holiday, file on the next business day.

## Private Delivery Services

You can use certain private delivery services designated by the IRS to meet the "timely mailing as timely filing/paying" rule for tax returns and payments. The most recent list of designated private delivery services was published by the IRS in September 2002. The list includes only the following:

- Airborne Express (Airborne): Overnight Air Express Service, Next Afternoon Service, Second Day Service.
- DHL Worldwide Express (DHL): DHL "Same Day" Service, DHL USA Overnight.
- Federal Express (FedEx): FedEx Priority Overnight, FedEx Standard Overnight, FedEx 2Day, FedEx International Priority, FedEx International First.
- United Parcel Service (UPS): UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, UPS 2nd Day Air A.M., UPS Worldwide Express Plus, UPS Worldwide Express.

The private delivery service can tell you how to get written proof of the mailing date.

## Extension of Time To File

**Estates.** Use **Form 2758**, Application for Extension of Time To File Certain Excise, Income, Information, and Other Returns, to apply for an extension of time to file.

**Trusts.** Use **Form 8736**, Application for Automatic Extension of Time To File U.S. Return for a Partnership, REMIC, or for Certain Trusts, to request an automatic 3-month extension of time to file.

If more time is needed, file **Form 8800**, Application for Additional Extension of Time To File U.S. Return for a Partnership, REMIC, or for Certain Trusts, for an additional extension of up to 3 months. To obtain this additional extension of time to file, you must show reasonable cause for the additional time you are requesting. Form 8800 must be filed by the extended due date for Form 1041.

## Period Covered

File the 2003 return for calendar year 2003 and fiscal years beginning in 2003 and ending in 2004. If the return is for a fiscal year or a short tax year (less than 12 months), fill in the tax year space at the top of the form.

The 2003 Form 1041 may also be used for a tax year beginning in 2004 if:

1. The estate or trust has a tax year of less than 12 months that begins and ends in 2004 and
2. The 2004 Form 1041 is not available by the time the estate or trust is required to file its tax return. However, the estate or trust must show its 2004 tax year on the 2003 Form 1041 and incorporate any tax law changes that are effective for tax years beginning after December 31, 2003.

## Who Must Sign

### Fiduciary

The fiduciary, or an authorized representative, must sign Form 1041. If there are joint fiduciaries, only one is required to sign the return.

A financial institution that submitted estimated tax payments for trusts for which it is the trustee must enter its employer identification number (EIN) in the space provided for the EIN of the fiduciary. Do not enter the EIN of the trust. For this purpose, a financial institution is one that maintains a Treasury Tax and Loan account. If you are an attorney or other individual functioning in a fiduciary capacity, leave this space blank. **Do not** enter your individual social security number (SSN).

If you, as fiduciary, fill in Form 1041, leave the Paid Preparer's space blank. If someone prepares this return and does not charge you, that person should not sign the return.

### Paid Preparer

Generally, anyone who is paid to prepare a tax return must sign the return and fill in

the other blanks in the Paid Preparer's Use Only area of the return.

The person required to sign the return must complete the required preparer information and:

- Sign it in the space provided for the preparer's signature. A facsimile signature is acceptable.
- Give you a copy of the return for your records.

### Paid Preparer Authorization

If the fiduciary wants to allow the IRS to discuss the estate's or trust's 2003 tax return with the paid preparer who signed it, check the "Yes" box in the signature area of the return. This authorization applies only to the individual whose signature appears in the "Paid Preparer's Use Only" section of the estate's or trust's return. It does not apply to the firm, if any, shown in that section.

If the "Yes" box is checked, the fiduciary is authorizing the IRS to call the paid preparer to answer any questions that may arise during the processing of the estate's or trust's return. The fiduciary is also authorizing the paid preparer to:

- Give the IRS any information that is missing from the estate's or trust's return,
- Call the IRS for information about the processing of the estate's or trust's return or the status of its refund or payment(s), and
- Respond to certain IRS notices that the fiduciary has shared with the preparer about math errors, offsets, and return preparation. The notices will not be sent to the preparer.

The fiduciary is not authorizing the paid preparer to receive any refund check, bind the estate or trust to anything (including any additional tax liability), or otherwise represent the estate or trust before the IRS. If the fiduciary wants to expand the paid preparer's authorization, see **Pub. 947**, Practice Before the IRS and Power of Attorney.

The authorization cannot be revoked. However, the authorization will automatically end no later than the due date (without regard to extensions) for filing the estate's or trust's 2004 tax return.

### Accounting Methods

Figure taxable income using the method of accounting regularly used in keeping the estate's or trust's books and records. Generally, permissible methods include the cash method, the accrual method, or any other method authorized by the Internal Revenue Code. In all cases, the method used must clearly reflect income.

Generally, the estate or trust may change its accounting method (for income as a whole or for any material item) only by getting consent on **Form 3115**, Application for Change in Accounting Method. For more information, see **Pub. 538**, Accounting Periods and Methods.

### Accounting Periods

For a decedent's estate, the moment of death determines the end of the decedent's tax year and the beginning of the estate's tax year. As executor or administrator, you choose the estate's tax period when you file its first income tax return. The estate's first tax year may be any period of 12 months or less that ends on the last day of a month. If you select the last day of any month other than December, you are adopting a fiscal tax year.

To change the accounting period of an estate, get **Form 1128**, Application To Adopt, Change, or Retain a Tax Year.

Generally, a trust must adopt a calendar year. The following trusts are exempt from this requirement:

- A trust that is exempt from tax under section 501(a);
- A charitable trust described in section 4947(a)(1); and
- A trust that is treated as wholly owned by a grantor under the rules of sections 671 through 679.

### Rounding Off to Whole Dollars

You may round off cents to whole dollars on the estate's or trust's return and schedules. If you do round to whole dollars, you must round all amounts. To round, drop amounts under 50 cents and increase amounts from 50 to 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.

### Estimated Tax

Generally, an estate or trust must pay estimated income tax for 2004 if it expects to owe, after subtracting any withholding and credits, at least \$1,000 in tax, and it expects the withholding and credits to be less than the smaller of:

1. 90% of the tax shown on the 2004 tax return or
2. 100% of the tax shown on the 2003 tax return (110% of that amount if the estate's or trust's adjusted gross income on that return is more than \$150,000, and less than  $\frac{2}{3}$  of gross income for 2003 or 2004 is from farming or fishing).

However, if a return was not filed for 2003 or that return did not cover a full 12 months, item 2 does not apply.

For this purpose, include household employment taxes in the tax shown on the tax return, but **only** if **either** of the following is true:

- The estate or trust will have Federal income tax withheld for 2004 (see the instructions on page 19 for line 24e) or
- The estate or trust would be required to make estimated tax payments for 2004 even if it **did not** include household

employment taxes when figuring estimated tax.

### Exceptions

Estimated tax payments are not required from:

1. An estate of a domestic decedent or a domestic trust that had no tax liability for the full 12-month 2003 tax year;
2. A decedent's estate for any tax year ending before the date that is 2 years after the decedent's death; or
3. A trust that was treated as owned by the decedent if the trust will receive the residue of the decedent's estate under the will (or if no will is admitted to probate, the trust primarily responsible for paying debts, taxes, and expenses of administration) for any tax year ending before the date that is 2 years after the decedent's death.

For more information, see **Form 1041-ES**, Estimated Income Tax for Estates and Trusts.

### Electronic Deposits

A financial institution that maintains a Treasury Tax and Loan (TT&L) account, and acts as a fiduciary for at least 200 taxable trusts that are required to pay estimated tax, may be required to deposit the estimated tax payments electronically using the Electronic Federal Tax Payment System (EFTPS). The electronic deposit requirement applies in 2004 if:

- The total deposits of depository taxes (such as estimated, employment, or excise tax) in 2002 were more than \$200,000 or
- The fiduciary (on behalf of a trust) was required to use EFTPS in 2003.

If the fiduciary is required to use EFTPS on behalf of a trust and fails to do so, it may be subject to a 10% penalty.

A fiduciary that is not required to make electronic deposits of estimated tax on behalf of a trust may either use the payment vouchers (see Form 1041-ES) or voluntarily participate in EFTPS. To enroll in or get more information about EFTPS, call 1-800-555-4477 or 1-800-945-8400.

**Depositing on time.** For deposits made by EFTPS to be on time, the fiduciary must initiate the transaction at least 1 business day before the date the deposit is due.

### Section 643(g) Election

Fiduciaries of trusts that pay estimated tax may elect under section 643(g) to have any portion of their estimated tax payments allocated to any of the beneficiaries.

The fiduciary of a decedent's estate may make a section 643(g) election only for the final year of the estate.

See the instructions for line 24b on page 19 for more details.



## Interest and Penalties

### Interest

Interest is charged on taxes not paid by the due date, even if an extension of time to file is granted.

Interest is also charged on the failure-to-file penalty, the accuracy-related penalty, and the fraud penalty. The interest charge is figured at a rate determined under section 6621.

### Late Filing of Return

The law provides a penalty of 5% of the tax due for each month, or part of a month, the return is not filed up to a maximum of 25% of the tax due (15% for each month, or part of a month, up to a maximum of 75% if the failure to file is fraudulent). If the return is more than 60 days late, the minimum penalty is the smaller of \$100 or the tax due. The penalty will not be imposed if you can show that the failure to file on time was due to reasonable cause. If the failure is due to reasonable cause, attach an explanation to the return.

### Late Payment of Tax

Generally, the penalty for not paying tax when due is  $\frac{1}{2}$  of 1% of the unpaid amount for each month or part of a month it remains unpaid. The maximum penalty is 25% of the unpaid amount. The penalty applies to any unpaid tax on the return. Any penalty is in addition to interest charges on late payments.



*If you include interest or either of these penalties with your payment, identify and enter these amounts in the bottom margin of Form 1041, page 1. Do not include the interest or penalty amount in the balance of tax due on line 27.*

### Failure To Provide Information Timely

You must provide Schedule K-1 (Form 1041), on or before the day you are required to file Form 1041, to each beneficiary who receives a distribution of property or an allocation of an item of the estate.

For each failure to provide Schedule K-1 to a beneficiary when due and each failure to include on Schedule K-1 all the information required to be shown (or the inclusion of incorrect information), a \$50 penalty may be imposed with regard to each Schedule K-1 for which a failure occurs. The maximum penalty is \$100,000 for all such failures during a calendar year. If the requirement to report information is intentionally disregarded, each \$50 penalty is increased to \$100 or, if greater, 10% of the aggregate amount of items required to be reported, and the \$100,000 maximum does not apply.

The penalty will not be imposed if the fiduciary can show that not providing information timely was due to reasonable cause and not due to willful neglect.

### Underpaid Estimated Tax

If the fiduciary underpaid estimated tax, use **Form 2210**, Underpayment of Estimated Tax by Individuals, Estates, and Trusts, to figure any penalty. Enter the amount of any penalty on line 26, Form 1041.

### Trust Fund Recovery Penalty

This penalty may apply if certain excise, income, social security, and Medicare taxes that must be collected or withheld are not collected or withheld, or these taxes are not paid. These taxes are generally reported on Forms 720, 941, 943, or 945. The trust fund recovery penalty may be imposed on all persons who are determined by the IRS to have been **responsible** for collecting, accounting for, or paying over these taxes, and who acted willfully in not doing so. The penalty is equal to the unpaid trust fund tax. See the instructions for Form 720, **Pub. 15 (Circular E)**, Employer's Tax Guide, or **Pub. 51 (Circular A)**, Agricultural Employer's Tax Guide, for more details, including the definition of responsible persons.

### Other Penalties

Other penalties can be imposed for negligence, substantial understatement of tax, and fraud. See **Pub. 17**, Your Federal Income Tax, for details on these penalties.

## Other Forms That May Be Required

**Forms W-2** and **W-3**, Wage and Tax Statement; and Transmittal of Wage and Tax Statements.

**Form 56**, Notice Concerning Fiduciary Relationship.

**Form 706**, United States Estate (and Generation-Skipping Transfer) Tax Return; or **Form 706-NA**, United States Estate (and Generation-Skipping Transfer) Tax Return, Estate of nonresident not a citizen of the United States.

**Form 706-GS(D)**, Generation-Skipping Transfer Tax Return for Distributions.

**Form 706-GS(D-1)**, Notification of Distribution From a Generation-Skipping Trust.

**Form 706-GS(T)**, Generation-Skipping Transfer Tax Return for Terminations.

**Form 720**, Quarterly Federal Excise Tax Return. Use Form 720 to report environmental excise taxes, communications and air transportation taxes, fuel taxes, luxury tax on passenger vehicles, manufacturers' taxes, ship passenger tax, and certain other excise taxes.

**Caution:** See **Trust Fund Recovery Penalty** above.

**Form 926**, Return by a U.S. Transferor of Property to a Foreign Corporation. Use this form to report certain information required under section 6038B.

**Form 940** or **Form 940-EZ**, Employer's Annual Federal Unemployment (FUTA) Tax Return. The estate or trust may be liable for FUTA tax and may have to file Form 940 or 940-EZ if it paid wages of \$1,500 or more in any calendar quarter during the calendar year (or the preceding calendar year) or one or more employees worked for the estate or trust for some part of a day in any 20 different weeks during the calendar year (or the preceding calendar year).

**Form 941**, Employer's Quarterly Federal Tax Return. Employers must file this form quarterly to report income tax withheld on wages and employer and employee social security and Medicare taxes. Agricultural employers must file **Form 943**, Employer's Annual Tax Return for Agricultural Employees, instead of Form 941, to report income tax withheld and employer and employee social security and Medicare taxes on farmworkers.

**Caution:** See **Trust Fund Recovery Penalty** above.

**Form 945**, Annual Return of Withheld Federal Income Tax. Use this form to report income tax withheld from nonpayroll payments, including pensions, annuities, IRAs, gambling winnings, and backup withholding.

**Caution:** See **Trust Fund Recovery Penalty** above.

**Form 1040**, U.S. Individual Income Tax Return.

**Form 1040NR**, U.S. Nonresident Alien Income Tax Return.

**Form 1041-A**, U.S. Information Return—Trust Accumulation of Charitable Amounts.

**Forms 1042** and **1042-S**, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons; and Foreign Person's U.S. Source Income Subject to Withholding. Use these forms to report and transmit withheld tax on payments or distributions made to nonresident alien individuals, foreign partnerships, or foreign corporations to the extent such payments or distributions constitute gross income from sources within the United States that is not effectively connected with a U.S. trade or business. For more information, see sections 1441 and 1442, and **Pub. 515**, Withholding of Tax on Nonresident Aliens and Foreign Entities.

**Forms 1099-A, B, INT, LTC, MISC, MSA, OID, R, and S.** You may have to file these information returns to report acquisitions or abandonments of secured property; proceeds from broker and barter exchange transactions; interest payments; payments of long-term care and accelerated death benefits; miscellaneous income payments; distributions from an Archer MSA or Medicare + Choice MSA; original issue discount; distributions from pensions, annuities, retirement or profit-sharing plans, IRAs (including SEPs, SIMPLEs, Roth IRAs, Roth Conversions, and IRA recharacterizations), Coverdell ESAs,

insurance contracts, etc.; and proceeds from real estate transactions.

Also, use certain of these returns to report amounts received as a nominee on behalf of another person, except amounts reported to beneficiaries on Schedule K-1 (Form 1041).

**Form 8275, Disclosure Statement.** File Form 8275 to disclose items or positions, except those contrary to a regulation, that are not otherwise adequately disclosed on a tax return. The disclosure is made to avoid parts of the accuracy-related penalty imposed for disregard of rules or substantial understatement of tax. Form 8275 is also used for disclosures relating to preparer penalties for understatements due to unrealistic positions or disregard of rules.

**Form 8275-R, Regulation Disclosure Statement,** is used to disclose any item on a tax return for which a position has been taken that is contrary to Treasury regulations.

**Forms 8288 and 8288-A, U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests; and Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests.** Use these forms to report and transmit withheld tax on the sale of U.S. real property by a foreign person. Also, use these forms to report and transmit tax withheld from amounts distributed to a foreign beneficiary from a "U.S. real property interest account" that a domestic estate or trust is required to establish under Regulations section 1.1445-5(c)(1)(iii).

**Form 8300, Report of Cash Payments Over \$10,000 Received in a Trade or Business.** Generally, this form is used to report the receipt of more than \$10,000 in cash or foreign currency in one transaction (or a series of related transactions).

**Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships.** The estate or trust may have to file Form 8865 if it:

1. Controlled a foreign partnership (i.e., owned more than a 50% direct or indirect interest in a foreign partnership).

2. Owned at least a 10% direct or indirect interest in a foreign partnership while U.S. persons controlled that partnership.

3. Had an acquisition, disposition, or change in proportional interest in a foreign partnership that:

a. Increased its direct interest to at least 10%;

b. Reduced its direct interest of at least 10% to less than 10%; or

c. Changed its direct interest by at least a 10% interest.

4. Contributed property to a foreign partnership in exchange for a partnership interest if:

a. Immediately after the contribution, the estate or trust owned, directly or indirectly, at least a 10% interest in the foreign partnership or

b. The fair market value of the property the estate or trust contributed to the foreign partnership in exchange for a partnership interest, when added to other contributions of property made to the foreign partnership during the preceding 12-month period, exceeds \$100,000.

Also, the estate or trust may have to file Form 8865 to report certain dispositions by a foreign partnership of property it previously contributed to that foreign partnership if it was a partner at the time of the disposition.

For more details, including penalties for failing to file Form 8865, see Form 8865 and its separate instructions.

**Tax shelter disclosure statement.** Use **Form 8886, Reportable Transaction Disclosure Statement,** to disclose information for each reportable transaction in which the trust participated, directly or indirectly. Form 8886 must be filed for each tax year that the Federal income tax liability of the estate or trust is affected by its participation in the transaction. The following are reportable transactions.

- Any transaction the same as or substantially similar to tax avoidance transactions identified by the IRS.
- Any transaction offered under conditions of confidentiality.
- Any transaction for which the estate or trust has contractual protection against disallowance of the tax benefits.
- Any transaction resulting in a loss of at least \$2 million in any single year or \$4 million in any combination of years (\$50,000 in any single year if the loss is generated by a section 988 transaction).
- Any transaction resulting in a book-tax difference of more than \$10 million on a gross basis.
- Any transaction resulting in a tax credit of more than \$250,000, if the estate or trust held the asset generating the credit for less than 45 days.

Generally, these rules apply to transactions entered into after 2002. For the rules that apply to reportable transactions entered into before 2003, see Temporary Regulations section 1.6011-4T (as in effect before February 28, 2003).

See the Instructions for Form 8886 for more details and exceptions.

## Assembly and Attachments

Assemble any schedules, forms and/or attachments **behind** Form 1041 in the following order:

1. Schedule D (Form 1041),
2. Schedule H (Form 1040),
3. Form 4136,
4. All other schedules and forms, and
5. All attachments.

## Attachments

If you need more space on the forms or schedules, attach separate sheets. Use the same size and format as on the

printed forms. **But show the totals on the printed forms.**

Attach these separate sheets after all the schedules and forms. Enter the estate's or trust's EIN on each sheet.

Do not file a copy of the decedent's will or the trust instrument unless the IRS requests it.

## Additional Information

The following publications may assist you in preparing Form 1041.

**Pub. 550, Investment Income and Expenses,** and

**Pub. 559, Survivors, Executors, and Administrators.**

## Of Special Interest to Bankruptcy Trustees and Debtors-in-Possession

### Taxation of Bankruptcy Estates of an Individual


The bankruptcy estate that is created when an individual debtor files a petition under either chapter 7 or 11 of title 11 of the U.S. Code is treated as a separate taxable entity. The bankruptcy estate is administered by a trustee or a debtor-in-possession. If the case is later dismissed by the bankruptcy court, the individual debtor is treated as if the bankruptcy petition had never been filed.

A separate taxable entity is not created if a partnership or corporation files a petition under any chapter of title 11 of the U.S. Code.

### Who Must File

Every trustee (or debtor-in-possession) for an individual's bankruptcy estate under chapter 7 or 11 of title 11 of the U.S. Code must file a return if the bankruptcy estate has gross income of \$7,800 or more for tax years beginning in 2003.

Failure to do so may result in an estimated Request for Administrative Expenses being filed by the IRS in the bankruptcy proceeding or a motion to compel filing of the return.

 *The filing of a tax return for the bankruptcy estate does not relieve the individual debtor of his or her (or their) individual tax obligations.*

### Employer Identification Number

Every bankruptcy estate of an individual required to file a return must have its own EIN. The SSN of the individual debtor cannot be used as the EIN for the bankruptcy estate.

### Accounting Period

A bankruptcy estate is allowed to have a fiscal year. The period can be no longer than 12 months.

### When To File

File Form 1041 on or before the 15th day of the 4th month following the close of the

tax year. Use Form 2758 to apply for an extension of time to file.

## Disclosure of Return Information

Under section 6103(e)(5), tax returns of individual debtors who have filed for bankruptcy under chapters 7 or 11 of title 11 are, upon written request, open to inspection by or disclosure to the trustee.

The returns subject to disclosure to the trustee are those for the year the bankruptcy begins and prior years. Use **Form 4506**, Request for Copy or Transcript of Tax Form, to request copies of the individual debtor's tax returns.

If the bankruptcy case was not voluntary, disclosure cannot be made before the bankruptcy court has entered an order for relief, unless the court rules that the disclosure is needed for determining whether relief should be ordered.

## Transfer of Tax Attributes From the Individual Debtor to the Bankruptcy Estate

The bankruptcy estate succeeds to the following tax attributes of the individual debtor:

1. Net operating loss (NOL) carryovers;
  2. Charitable contributions carryovers;
  3. Recovery of tax benefit items;
  4. Credit carryovers;
  5. Capital loss carryovers;
  6. Basis, holding period, and character of assets;
  7. Method of accounting;
  8. Unused passive activity losses;
  9. Unused passive activity credits;
- and
10. Unused section 465 losses.

## Income, Deductions, and Credits

Under section 1398(c), the taxable income of the bankruptcy estate generally is figured in the same manner as an individual. The gross income of the bankruptcy estate includes any income included in property of the estate as defined in Bankruptcy Code section 541. Also included is gain from the sale of property. To figure gain, the trustee or debtor-in-possession must determine the correct basis of the property.

To determine whether any amount paid or incurred by the bankruptcy estate is allowable as a deduction or credit, or is treated as wages for employment tax purposes, treat the amount as if it were paid or incurred by the individual debtor in the same trade or business or other activity the debtor engaged in before the bankruptcy proceedings began.

**Administrative expenses.** The bankruptcy estate is allowed a deduction for any administrative expense allowed under section 503 of title 11 of the U.S. Code, and any fee or charge assessed under chapter 123 of title 28 of the U.S. Code, to the extent not disallowed under an Internal Revenue Code provision (e.g., section 263, 265, or 275).

**Administrative expense loss.** When figuring a net operating loss, nonbusiness deductions (including administrative expenses) are limited under section 172(d)(4) to the bankruptcy estate's nonbusiness income. The excess nonbusiness deductions are an administrative expense loss that may be carried back to each of the 3 preceding tax years and forward to each of the 7 succeeding tax years of the bankruptcy estate. The amount of an administrative expense loss that may be carried to any tax year is determined after the net operating loss deductions allowed for that year. An administrative expense loss is allowed only to the bankruptcy estate and cannot be carried to any tax year of the individual debtor.

**Carryback of net operating losses and credits.** If the bankruptcy estate itself incurs a net operating loss (apart from losses carried forward to the estate from the individual debtor), it can carry back its net operating losses not only to previous tax years of the bankruptcy estate, but also to tax years of the individual debtor prior to the year in which the bankruptcy proceedings began. Excess credits, such as the foreign tax credit, also may be carried back to pre-bankruptcy years of the individual debtor.

**Exemption.** For tax years beginning in 2003, a bankruptcy estate is allowed a personal exemption of \$3,050.

**Standard deduction.** For tax years beginning in 2003, a bankruptcy estate that does not itemize deductions is allowed a standard deduction of \$4,750.

**Discharge of indebtedness.** In a title 11 case, gross income does not include amounts that normally would be included in gross income resulting from the discharge of indebtedness. However, any amounts excluded from gross income must be applied to reduce certain tax attributes in a certain order. Attach **Form 982**, Reduction of Tax Attributes Due to Discharge of Indebtedness, to show the reduction of tax attributes.

## Tax Rate Schedule

Figure the tax for the bankruptcy estate using the tax rate schedule below. Enter the tax on Form 1040, line 41.

If taxable income is:

| Over —  | But not over — | The tax is:     | Of the amount over — |
|---------|----------------|-----------------|----------------------|
| \$0     | \$7,000        | 10%             | \$0                  |
| 7,000   | 28,400         | \$700.00 + 15%  | 7,000                |
| 28,400  | 57,325         | 3,910.00 + 25%  | 28,400               |
| 57,325  | 87,350         | 11,141.25 + 28% | 57,325               |
| 87,350  | 155,975        | 19,548.25 + 33% | 87,350               |
| 155,975 | -----          | 42,194.50 + 35% | 155,975              |

## Prompt Determination of Tax Liability

To request a prompt determination of the tax liability of the bankruptcy estate, the trustee or debtor-in-possession must file a written application for the determination with the IRS. Send the request to the Small Business/Self-Employed Insolvency Territory Manager for the territory in which the bankruptcy case is pending. The application must be submitted in duplicate and executed under the penalties of perjury. The trustee or debtor-in-possession must submit with the application an **exact copy** of the return (or returns) filed by the trustee with the IRS for a completed tax period, and a statement of the name and location of the office where the return was filed. The envelope should be marked, "Request for Prompt Determination. DO NOT OPEN IN MAILROOM."

The IRS will notify the trustee or debtor-in-possession within 60 days from receipt of the application whether the return filed by the trustee or debtor-in-possession has been selected for examination or has been accepted as filed. If the return is selected for examination, it will be examined as soon as possible. The IRS will notify the trustee or debtor-in-possession of any tax due within 180 days from receipt of the application or within any additional time permitted by the bankruptcy court.

See Rev. Proc. 81-17, 1981-1 C.B. 688.

## Special Filing Instructions for Bankruptcy Estates

Use Form 1041 only as a transmittal for Form 1040. In the top margin of Form 1040 write "Attachment to Form 1041. DO NOT DETACH." Attach Form 1040 to Form 1041. Complete only the identification area at the top of Form 1041. Enter the name of the individual debtor in the following format: "John Q. Public Bankruptcy Estate." Beneath, enter the name of the trustee in the following format: "Avery Snow, Trustee." In item D, enter the date the petition was filed or the date of conversion to a chapter 7 or 11 case.

Enter on Form 1041, line 23, the total tax from line 60 of Form 1040. Complete lines 24 through 29 of Form 1041, and sign and date it.

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## Specific Instructions

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### Name of Estate or Trust

Copy the exact name of the estate or trust from the **Form SS-4**, Application for Employer Identification Number, that you used to apply for the EIN.

If a grantor type trust (discussed below), write the name, identification number, and address of the grantor(s) or other owner(s) in parentheses after the name of the trust.

### Name and Title of Fiduciary

Enter the name and title of the fiduciary. If the name entered is different than the name on the prior year's return, see **Change in Fiduciary's Name** on page 13.

### Address

Include the suite, room, or other unit number after the street address.

If the Post Office does not deliver mail to the street address and the fiduciary has a P.O. box, show the box number instead of the street address.

If you change your address after filing Form 1041, use **Form 8822**, Change of Address, to notify the IRS.

If you have a new address and have not filed Form 8822, be sure to check the box in **F** for "Change in fiduciary's address."

### A. Type of Entity

Check the appropriate box that describes the entity for which you are filing the return.

If only a portion of a trust is a grantor type trust or if only a portion of an electing small business trust is the S portion, then more than one box can be checked.

**Note:** *There are special filing requirements for grantor type trusts, pooled income funds, electing small business trusts, and bankruptcy estates. See **Special Filing Instructions for Grantor Type Trusts, Pooled Income Funds, and Electing Small Business Trusts** on page 5, or **Of Special Interest to Bankruptcy Trustees and Debtors-in-Possession** on page 10.*

### Decedent's Estate

An estate of a deceased person is a taxable entity separate from the decedent. It generally continues to exist until the final distribution of the assets of the estate is made to the heirs and other beneficiaries. The income earned from the property of the estate during the period of administration or settlement must be accounted for and reported by the estate.

### Simple Trust

A trust may qualify as a simple trust if:

1. The trust instrument requires that all income must be distributed currently;
2. The trust instrument does not provide that any amounts are to be paid, permanently set aside, or used for charitable purposes; and
3. The trust does not distribute amounts allocated to the corpus of the trust.

### Complex Trust

A complex trust is any trust that does not qualify as a simple trust as explained above.

### Qualified Disability Trust

A qualified disability trust is any nongrantor trust:

1. Described in 42 U.S.C. 1396p(c)(2)(B)(iv) and established solely for the benefit of an individual under 65 years of age who is disabled and
2. All the beneficiaries of which are determined by the Commissioner of Social Security to have been disabled for some part of the tax year within the meaning of 42 U.S.C. 1382c(a)(3).

A trust will not fail to meet **2** above just because the trust's corpus may revert to a person who is not disabled after the trust ceases to have any disabled beneficiaries.

### ESBT (S Portion Only)

The S portion of an electing small business trust (ESBT) is the portion of the trust that consists of S corporation stock and that is not treated as owned by the grantor or another person. See page 7 of the instructions for more information about an ESBT.

### Grantor Type Trust

A grantor type trust is a legal trust under applicable state law that is not recognized as a separate taxable entity for income tax purposes because the grantor or other substantial owners have not relinquished complete dominion and control over the trust.

Generally, for transfers made in trust after March 1, 1986, the grantor is treated as the owner of any portion of a trust in which he or she has a reversionary interest in either the income or corpus therefrom, if, as of the inception of that portion of the trust, the value of the reversionary interest is more than 5% of the value of that portion. Also, the grantor is treated as holding any power or interest that was held by either the grantor's spouse at the time that the power or interest was created or who became the grantor's spouse after the creation of that power or interest.

**Mortgage pools.** The trustee of a mortgage pool, such as the Federal National Mortgage Association, collects principal and interest payments on each mortgage and makes distributions to the certificate holders. Each pool is

considered a grantor type trust, and each certificate holder is treated as the owner of an undivided interest in the entire trust under the grantor trust rules. Certificate holders must report their proportionate share of the mortgage interest and other items of income on their individual tax returns.

**Pre-need funeral trusts.** The purchasers of pre-need funeral services are the grantors and the owners of pre-need funeral trusts established under state laws. See Rev. Rul. 87-127, 1987-2 C.B. 156. However, the trustees of pre-need funeral trusts can elect to file the return and pay the tax for qualified funeral trusts. For more information, see **Form 1041-QFT**, U.S. Income Tax Return for Qualified Funeral Trusts.

**Nonqualified deferred compensation plans.** Taxpayers may adopt and maintain grantor trusts in connection with nonqualified deferred compensation plans (sometimes referred to as "rabbi trusts"). Rev. Proc. 92-64, 1992-2 C.B. 422, provides a "model grantor trust" for use in rabbi trust arrangements. The procedure also provides guidance for requesting rulings on the plans that use these trusts.

### Bankruptcy Estate

A chapter 7 or 11 bankruptcy estate is a separate and distinct taxable entity from the individual debtor for Federal income tax purposes. See **Of Special Interest to Bankruptcy Trustees and Debtors-in-Possession** on page 10.

For more information, see section 1398 and **Pub. 908**, Bankruptcy Tax Guide.

### Pooled Income Fund

A pooled income fund is a split-interest trust with a remainder interest for a public charity and a life income interest retained by the donor or for another person. The property is held in a pool with other pooled income fund property and does not include any tax-exempt securities. The income for a retained life interest is figured using the yearly rate of return earned by the trust. See section 642(c) and the related regulations for more information.

### B. Number of Schedules K-1 Attached

Every trust or decedent's estate claiming an income distribution deduction on page 1, line 18, must enter the number of Schedules K-1 (Form 1041) that are attached to Form 1041.

### C. Employer Identification Number

Every estate or trust that is required to file Form 1041 must have an EIN. An EIN may be applied for:

- Online by clicking on the EIN link at [www.irs.gov/businesses/small](http://www.irs.gov/businesses/small). The EIN is issued immediately once the application information is validated.

- By telephone at 1-800-829-4933 from 7:30 a.m. to 5:30 p.m. in the fiduciary's local time zone.

- By mailing or faxing **Form SS-4**, Application for Employer Identification Number.

If the estate or trust has not received its EIN by the time the return is due, write "Applied for" in the space for the EIN. For more details, see **Pub. 583**, Starting a Business and Keeping Records.

If you are filing a return for a **mortgage pool**, such as one created under the mortgage-backed security programs administered by the Federal National Mortgage Association ("Fannie Mae") or the Government National Mortgage Association ("Ginnie Mae"), the EIN stays with the pool if that pool is traded from one financial institution to another.

## D. Date Entity Created

Enter the date the trust was created, or, if a decedent's estate, the date of the decedent's death.

## E. Nonexempt Charitable and Split-Interest Trusts

### Section 4947(a)(1) Trust

Check this box if the trust is a nonexempt charitable trust within the meaning of section 4947(a)(1).

A nonexempt charitable trust is a trust:

- That is not exempt from tax under section 501(a);
- In which all of the unexpired interests are devoted to one or more charitable purposes described in section 170(c)(2)(B); and
- For which a deduction was allowed under section 170 (for individual taxpayers) or similar Code section for personal holding companies, foreign personal holding companies, or estates or trusts (including a deduction for estate or gift tax purposes).

**Nonexempt charitable trust treated as a private foundation.** If a nonexempt charitable trust is treated as though it were a private foundation under section 509, then the fiduciary must file **Form 990-PF**, Return of Private Foundation, in addition to Form 1041.

If a nonexempt charitable trust is treated as though it were a private foundation, and it has no taxable income under Subtitle A, it may file Form 990-PF instead of Form 1041 to meet its section 6012 filing requirement. But, be sure to answer Statement 13, on Part VII-A of Form 990-PF.

**Excise taxes.** If a nonexempt charitable trust is treated as a private foundation, then it is subject to the same excise taxes under chapters 41 and 42 that a private foundation is subject to. If the nonexempt charitable trust is liable for any of these taxes (except the section 4940 tax), then it reports these taxes on **Form 4720**, Return of Certain Excise

Taxes on Charities and Other Persons Under Chapters 41 and 42 of the Internal Revenue Code. Taxes paid by the trust on Form 4720 or on Form 990-PF (the section 4940 tax) **cannot** be taken as a deduction on Form 1041.

### Not a Private Foundation

Check this box if the nonexempt charitable trust (section 4947(a)(1)) is not treated as a private foundation under section 509. For more information, see Regulations section 53.4947-1.

**Other returns that must be filed.** If a nonexempt charitable trust is not treated as though it were a private foundation, the fiduciary must file, in addition to Form 1041, **Form 990** (or **Form 990-EZ**), Return of Organization Exempt From Income Tax, and **Schedule A (Form 990 or 990-EZ)**, Organization Exempt Under Section 501(c)(3), if the trust's gross receipts are normally more than \$25,000.

If a nonexempt charitable trust is not treated as though it were a private foundation, and it has no taxable income under Subtitle A, it can file either Form 990 or Form 990-EZ instead of Form 1041 to meet its section 6012 filing requirement.

### Section 4947(a)(2) Trust

Check this box if the trust is a split-interest trust described in section 4947(a)(2).

A split-interest trust is a trust that:

- Is not exempt from tax under section 501(a);
- Has some unexpired interests that are devoted to purposes other than religious, charitable, or similar purposes described in section 170(c)(2)(B); and
- Has amounts transferred in trust after May 26, 1969, for which a deduction was allowed under section 170 (for individual taxpayers) or similar Code section for personal holding companies, foreign personal holding companies, or estates or trusts (including a deduction for estate or gift tax purposes).

**Other returns that must be filed.** The fiduciary of a split-interest trust must file Form 5227 (for amounts transferred in trust after May 26, 1969); and Form 1041-A if the trust's governing instrument does not require that all of the trust's income be distributed currently.

If a split-interest trust has any unrelated business taxable income, however, it must file Form 1041 to report all of its income and to pay any tax due.

## F. Initial Return, Amended Return, Final Return, or Change in Fiduciary's Name or Address

### Amended Return

If you are filing an amended Form 1041:

- Check the "Amended return" box,
- Complete the entire return,

- Correct the appropriate lines with the new information, and

- Refigure the estate's or trust's tax liability.

If the total tax on line 23 is larger on the amended return than on the original return, you generally should pay the difference with the amended return. However, you should adjust this amount if there is any increase or decrease in the total payments shown on line 25.

Attach a sheet that explains the reason for the amendments and identifies the lines and amounts being changed on the amended return.

**Amended Schedule K-1 (Form 1041).** If the amended return results in a change to income, or a change in distribution of any income or other information provided to a beneficiary, an amended Schedule K-1 (Form 1041) must also be filed with the amended Form 1041 and given to each beneficiary. Check the "Amended K-1" box at the top of the amended Schedule K-1.

### Final Return

Check this box if this is a final return because the estate or trust has terminated. Also, check the "Final K-1" box at the top of Schedule K-1.

If, on the final return, there are excess deductions, an unused capital loss carryover, or a net operating loss carryover, see the instructions for Schedule K-1, lines 13a through 13e, on page 41.

### Change in Fiduciary's Name

If the fiduciary's name entered is different than the name on the prior year's return (or the Form 56 if no prior return), be sure to check this box. Also, file Form 56 if you checked this box and you have not filed a Form 56 or otherwise notified the IRS that you are a fiduciary for the estate or trust.

### Change in Fiduciary's Address

Check this box if the fiduciary's address is different than the one entered on the prior return (or Form 56 if no prior return) and you have not filed Form 8822. If the fiduciary's address changed after filing Form 1041, use Form 8822 to notify the IRS unless the change was due to the creation or termination of a fiduciary relationship, in which case you should file a Form 56.

## G. Pooled Mortgage Account

If you bought a pooled mortgage account during the year and still have that pool at the end of the tax year, check the "Bought" box and enter the date of purchase. If you sold a pooled mortgage account that was purchased during this, or a previous, tax year, check the "Sold" box and enter the date of sale. If you neither bought nor sold a pooled mortgage account, skip this item.

## Income

### Special Rule for Blind Trust

If you are reporting income from a qualified blind trust (under the Ethics in Government Act of 1978), do not identify the payer of any income to the trust but complete the rest of the return as provided in the instructions. Also write "Blind Trust" at the top of page 1.

### Extraterritorial Income Exclusion

The estate or trust may exclude extraterritorial income to the extent of qualifying foreign trade income. For details and to figure the amount of the exclusion, see **Form 8873**, Extraterritorial Income Exclusion, and its separate instructions. The estate or trust must report the extraterritorial income exclusion on line 15a of Form 1041, page 1.

Although the extraterritorial income exclusion is entered on line 15a, it is an exclusion from income and should be treated as tax-exempt income when completing other parts of the return.

### Line 1—Interest Income

Report the estate's or trust's share of all taxable interest income that was received during the tax year. Examples of taxable interest include interest from:

- Accounts (including certificates of deposit and money market accounts) with banks, credit unions, and thrift institutions.
- Notes, loans, and mortgages.
- U.S. Treasury bills, notes, and bonds.
- U.S. savings bonds.
- Original issue discount.
- Income received as a regular interest holder of a real estate mortgage investment conduit (REMIC).

For taxable bonds acquired after 1987, amortizable bond premium is treated as an offset to the interest income instead of as a separate interest deduction. See Pub. 550.

For the year of the decedent's death, Forms 1099-INT issued in the decedent's name may include interest income earned after the date of death that should be reported on the income tax return of the decedent's estate. When preparing the decedent's final income tax return, report on line 1 of Schedule B (Form 1040) or Schedule 1 (Form 1040A) the total interest shown on Form 1099-INT. Under the last entry on line 1, subtotal all the interest reported on line 1. Below the subtotal, write "Form 1041" and the name and address shown on Form 1041 for the decedent's estate. Also, show the part of the interest reported on Form 1041 and subtract it from the subtotal.

### Line 2a—Ordinary Dividends

Report the estate's or trust's share of all ordinary dividends received during the tax year.

For the year of the decedent's death, Forms 1099-DIV issued in the decedent's name may include dividends earned after the date of death that should be reported

on the income tax return of the decedent's estate. When preparing the decedent's final income tax return, report on line 5 of Schedule B (Form 1040) or Schedule 1 (Form 1040A) the ordinary dividends shown on Form 1099-DIV. Under the last entry on line 5, subtotal all the dividends reported on line 5. Below the subtotal, write "Form 1041" and the name and address shown on Form 1041 for the decedent's estate. Also, show the part of the ordinary dividends reported on Form 1041 and subtract it from the subtotal.

**Note:** Report capital gain distributions on Schedule D (Form 1041), line 9.

### Line 2b—Qualified Dividends

Enter the beneficiary's allocable share of qualified dividends on line 2b(1) and enter the estate's or trust's allocable share on line 2b(2). If the estate or trust received qualified dividends that were derived from income in respect of a decedent, you must reduce the amount on line 2b(2) by the portion of the estate tax deduction claimed on Form 1041, page 1, line 19, that is attributable to those qualified dividends. Do **not** reduce the amounts on line 2b by any other allocable expenses.

Qualified dividends are eligible for a lower tax rate than other ordinary income. Generally, these dividends are reported to the estate or trust in box 1b of Form(s) 1099-DIV. See Pub. 550 for the definition of qualified dividends if the estate or trust received dividends not reported on Form 1099-DIV.

**Exception.** Some dividends may be reported to the estate or trust as qualified dividends in box 1b of Form 1099-DIV but are not qualified dividends. These include:

- Dividends received on any share of stock that the estate or trust held for less than 61 days during the 120-day period that began 60 days before the ex-dividend date. The ex-dividend date is the first date following the declaration of a dividend on which the purchaser of a stock is not entitled to receive the next dividend payment. When counting the number of days the stock was held, include the day the estate or trust disposed of the stock but not the day it acquired the stock. However, you cannot count certain days during which the estate's or trust's risk of loss was diminished. See Pub. 550 for more details.
- Dividends attributable to periods totaling more than 366 days that the estate or trust received on any share of preferred stock held for less than 91 days during the 180-day period that began 90 days before the ex-dividend date. When counting the number of days the stock was held, include the day the estate or trust disposed of the stock but not the day it acquired the stock. However, you cannot count certain days during which the estate's or trust's risk of loss was diminished. See Pub. 550 for more details. Preferred dividends attributable to

periods totaling less than 367 days are subject to the 61-day holding period rule above.

- Dividends on any share of stock to the extent that the estate or trust is under an obligation (including a short sale) to make related payments with respect to positions in substantially similar or related property.
- Payments in lieu of dividends, but only if you know or have reason to know that the payments are not qualified dividends.



*If you have an entry on line 2b(2), be sure you use Schedule D (Form 1041) or the Qualified Dividends Tax Worksheet, whichever applies, to figure the estate's or trust's tax. Figuring the estate's or trust's tax liability in this manner will usually result in a lower tax.*

### Line 3—Business Income or (Loss)

If the estate or trust operated a business, report the income and expenses on **Schedule C (Form 1040)**, Profit or Loss From Business (or **Schedule C-EZ (Form 1040)**, Net Profit From Business). Enter the net profit or (loss) from Schedule C (or Schedule C-EZ) on line 3.

### Line 4—Capital Gain or (Loss)

Enter the gain from Schedule D (Form 1041), Part III, line 16a, column (3); or the loss from Part IV, line 17.



**Do not substitute Schedule D (Form 1040) for Schedule D (Form 1041).**

### Line 5—Rents, Royalties, Partnerships, Other Estates and Trusts, etc.

Use **Schedule E (Form 1040)**, Supplemental Income and Loss, to report the estate's or trust's share of income or (losses) from rents, royalties, partnerships, S corporations, other estates and trusts, and REMICs. Enter the net profit or (loss) from Schedule E on line 5. See the instructions for Schedule E (Form 1040) for reporting requirements.

If the estate or trust received a Schedule K-1 from a partnership, S corporation, or other flow-through entity, use the corresponding lines on Form 1041 to report the interest, dividends, capital gains, etc., from the flow-through entity.

### Line 6—Farm Income or (Loss)

If the estate or trust operated a farm, use **Schedule F (Form 1040)**, Profit or Loss From Farming, to report farm income and expenses. Enter the net profit or (loss) from Schedule F on line 6.

### Line 7—Ordinary Gain or (Loss)

Enter from line 18, **Form 4797**, Sales of Business Property, the ordinary gain or loss from the sale or exchange of property other than capital assets and also from involuntary conversions (other than casualty or theft).

## Line 8—Other Income

Enter other items of income not included on lines 1, 2a, and 3 through 7. List the type and amount on an attached schedule if the estate or trust has more than one item.

Items to be reported on line 8 include:

- Unpaid compensation received by the decedent's estate that is income in respect of a decedent.
- Any part of a total distribution shown on **Form 1099-R**, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., that is treated as ordinary income. For more information, see the separate instructions for **Form 4972**, Tax on Lump-Sum Distributions.

## Deductions

### Depreciation, Depletion, and Amortization

A trust or decedent's estate is allowed a deduction for depreciation, depletion, and amortization only to the extent the deductions are not apportioned to the beneficiaries. An estate or trust is not allowed to make an election under section 179 to expense certain tangible property.

The estate's or trust's share of depreciation, depletion, and amortization should be reported on the appropriate lines of Schedule C (or C-EZ), E, or F (Form 1040), the net income or loss from which is shown on line 3, 5, or 6 of Form 1041. If the deduction is not related to a specific business or activity, then report it on line 15a.

**Depreciation.** For a decedent's estate, the depreciation deduction is apportioned between the estate and the heirs, legatees, and devisees on the basis of the estate's income allocable to each.

For a trust, the depreciation deduction is apportioned between the income beneficiaries and the trust on the basis of the trust income allocable to each, unless the governing instrument (or local law) requires or permits the trustee to maintain a depreciation reserve. If the trustee is required to maintain a reserve, the deduction is first allocated to the trust, up to the amount of the reserve. Any excess is allocated among the beneficiaries in the same manner as the trust's accounting income. See Regulations section 1.167(h)-1(b).

**Depletion.** For mineral or timber property held by a decedent's estate, the depletion deduction is apportioned between the estate and the heirs, legatees, and devisees on the basis of the estate's income from such property allocable to each.

For mineral or timber property held in trust, the depletion deduction is apportioned between the income beneficiaries and the trust based on the trust income from such property allocable to each, unless the governing instrument (or local law) requires or permits the

trustee to maintain a reserve for depletion. If the trustee is required to maintain a reserve, the deduction is first allocated to the trust, up to the amount of the reserve. Any excess is allocated among the beneficiaries in the same manner as the trust's accounting income. See Regulations section 1.611-1(c)(4).

**Amortization.** The deduction for amortization is apportioned between an estate or trust and its beneficiaries under the same principles for apportioning the deductions for depreciation and depletion.

The deduction for the amortization of reforestation expenditures under section 194 is allowed only to an estate.

### Allocation of Deductions for Tax-Exempt Income

Generally, no deduction that would otherwise be allowable is allowed for any expense (whether for business or for the production of income) that is allocable to tax-exempt income. Examples of tax-exempt income include:

- Certain death benefits (section 101);
- Interest on state or local bonds (section 103);
- Compensation for injuries or sickness (section 104); and
- Income from discharge of indebtedness in a title 11 case (section 108).

**Exception.** State income taxes and business expenses that are allocable to tax-exempt interest are deductible.

Expenses that are directly allocable to tax-exempt income are allocated only to tax-exempt income. A reasonable proportion of expenses indirectly allocable to both tax-exempt income and other income must be allocated to each class of income.

### Deductions That May Be Allowable for Estate Tax Purposes

Administration expenses and casualty and theft losses deductible on Form 706 may be deducted, to the extent otherwise deductible for income tax purposes, on Form 1041 if the fiduciary files a statement waiving the right to deduct the expenses and losses on Form 706. The statement must be filed before the expiration of the statutory period of limitations for the tax year the deduction is claimed. See Pub. 559 for more information.

### Accrued Expenses

Generally, an accrual basis taxpayer can deduct accrued expenses in the tax year that: **(a)** all events have occurred that determine the liability; and **(b)** the amount of the liability can be figured with reasonable accuracy. However, all the events that establish liability are treated as occurring only when economic performance takes place. There are exceptions for recurring items. See section 461(h).

## Limitations on Deductions

### At-Risk Loss Limitations

Generally, the amount the estate or trust has "at risk" limits the loss it can deduct for any tax year. Use **Form 6198**, At-Risk Limitations, to figure the deductible loss for the year and file it with Form 1041. For more information, see **Pub. 925**, Passive Activity and At-Risk Rules.

### Passive Activity Loss and Credit Limitations

**In general.** Section 469 and the regulations thereunder generally limit losses from passive activities to the amount of income derived from all passive activities. Similarly, credits from passive activities are generally limited to the tax attributable to such activities. These limitations are first applied at the estate or trust level.

Generally, an activity is a passive activity if it involves the conduct of any trade or business, and the taxpayer does not materially participate in the activity. Passive activities do not include working interests in oil and gas properties. See section 469(c)(3).

**Note:** *Material participation standards for estates and trusts have not been established by regulations.*

For a grantor trust, material participation is determined at the grantor level.

If the estate or trust distributes an interest in a passive activity, the basis of the property immediately before the distribution is increased by the passive activity losses allocable to the interest, and such losses cannot be deducted. See section 469(j)(12).

**Note:** *Losses from passive activities are first subject to the at-risk rules. When the losses are deductible under the at-risk rules, the passive activity rules then apply.*

**Rental activities.** Generally, rental activities are passive activities, whether or not the taxpayer materially participates. However, certain taxpayers who materially participate in real property trades or businesses are not subject to the passive activity limitations on losses from rental real estate activities in which they materially participate. For more details, see section 469(c)(7).

For tax years of an estate ending less than 2 years after the decedent's date of death, up to \$25,000 of deductions and deduction equivalents of credits from rental real estate activities in which the decedent actively participated are allowed. Any excess losses and/or credits are suspended for the year and carried forward.

**Portfolio income.** Portfolio income is not treated as income from a passive activity, and passive losses and credits generally may not be applied to offset it. Portfolio income generally includes interest, dividends, royalties, and income from

annuities. Portfolio income of an estate or trust must be accounted for separately.

**Forms to file.** See **Form 8582**, Passive Activity Loss Limitations, to figure the amount of losses allowed from passive activities. See **Form 8582-CR**, Passive Activity Credit Limitations, to figure the amount of credit allowed for the current year.

## Transactions Between Related Taxpayers

Under section 267, a trust that uses the accrual method of accounting may only deduct business expenses and interest owed to a related party in the year the payment is included in the income of the related party. For this purpose, a related party includes:

1. A grantor and a fiduciary of any trust;
2. A fiduciary of a trust and a fiduciary of another trust, if the same person is a grantor of both trusts;
3. A fiduciary of a trust and a beneficiary of such trust;
4. A fiduciary of a trust and a beneficiary of another trust, if the same person is a grantor of both trusts;
5. A fiduciary of a trust and a corporation more than 50% in value of the outstanding stock of which is owned, directly or indirectly, by or for the trust or by or for a person who is a grantor of the trust; and
6. An executor of an estate and a beneficiary of that estate, except for a sale or exchange to satisfy a pecuniary bequest (i.e., a bequest of a sum of money).

## Line 10—Interest

Enter the amount of interest (subject to limitations) paid or incurred by the estate or trust on amounts borrowed by the estate or trust, or on debt acquired by the estate or trust (e.g., outstanding obligations from the decedent) that is not claimed elsewhere on the return.

If the proceeds of a loan were used for more than one purpose (e.g., to purchase a portfolio investment and to acquire an interest in a passive activity), the fiduciary must make an interest allocation according to the rules in Temporary Regulations section 1.163-8T.

Do not include interest paid on indebtedness incurred or continued to purchase or carry obligations on which the interest is wholly exempt from income tax.

Personal interest is not deductible. Examples of personal interest include interest paid on:

- Revolving charge accounts used to purchase personal use property.
- Personal notes for money borrowed from a bank, credit union, or other person.
- Installment loans on personal use property.
- Underpayments of Federal, state, or local income taxes.

Interest that is paid or incurred on indebtedness allocable to a trade or business (including a rental activity) should be deducted on the appropriate line of Schedule C (or C-EZ), E, or F (Form 1040), the net income or loss from which is shown on line 3, 5, or 6 of Form 1041.

Types of interest to include on line 10 are:

1. Any investment interest (subject to limitations—see below);
2. Any qualified residence interest (see below); and
3. Any interest payable under section 6601 on any unpaid portion of the estate tax attributable to the value of a reversionary or remainder interest in property for the period during which an extension of time for payment of such tax is in effect.

**Investment interest.** Generally, investment interest is interest (including amortizable bond premium on taxable bonds acquired after October 22, 1986, but before January 1, 1988) that is paid or incurred on indebtedness that is properly allocable to property held for investment. Investment interest does not include any qualified residence interest, or interest that is taken into account under section 469 in figuring income or loss from a passive activity.

Generally, net investment income is the excess of investment income over investment expenses. Investment expenses are those expenses (other than interest) allowable after application of the 2% floor on miscellaneous itemized deductions.

The amount of the investment interest deduction may be limited. Use **Form 4952**, Investment Interest Expense Deduction, to figure the allowable investment interest deduction.

If you must complete Form 4952, check the box on line 10 of Form 1041 and attach Form 4952. Then, add the deductible investment interest to the other types of deductible interest and enter the total on line 10.

**Qualified residence interest.** Interest paid or incurred by an estate or trust on indebtedness secured by a qualified residence of a beneficiary of an estate or trust is treated as qualified residence interest if the residence would be a qualified residence (i.e., the principal residence or the second residence selected by the beneficiary) if owned by the beneficiary. The beneficiary must have a present interest in the estate or trust or an interest in the residuary of the estate or trust. See **Pub. 936**, Home Mortgage Interest Deduction, for an explanation of the general rules for deducting home mortgage interest.

See section 163(h)(3) for a definition of qualified residence interest and for limitations on indebtedness.

## Line 11—Taxes

Enter any deductible taxes paid or incurred during the tax year that are not deductible elsewhere on Form 1041.

Deductible taxes include:


- State and local income or real property taxes.
- The generation-skipping transfer (GST) tax imposed on income distributions.

**Do not** deduct:

- Federal income taxes.
- Estate, inheritance, legacy, succession, and gift taxes.
- Federal duties and excise taxes.
- State and local sales taxes. Instead, treat these taxes as part of the cost of the property.

## Line 12—Fiduciary Fees

Enter the deductible fees paid or incurred to the fiduciary for administering the estate or trust during the tax year.

 *Fiduciary fees deducted on Form 706 cannot be deducted on Form 1041.*

## Line 15a—Other Deductions Not Subject to the 2% Floor

Attach your own schedule, listing by type and amount, all allowable deductions that are not deductible elsewhere on Form 1041.

Do not include any losses on worthless bonds and similar obligations and nonbusiness bad debts. Report these losses on Schedule D (Form 1041).

Do not deduct medical or funeral expenses on Form 1041. Medical expenses of the decedent paid by the estate may be deductible on the decedent's income tax return for the year incurred. See section 213(c). Funeral expenses are deductible **only** on Form 706.

The following are examples of deductions that are reported on line 15a.

**Bond premium(s).** For taxable bonds acquired before October 23, 1986, if the fiduciary elected to amortize the premium, report the amortization on this line. You cannot deduct the amortization for tax-exempt bonds. In all cases where the fiduciary has made an election to amortize the premium, the basis must be reduced by the amount of amortization.

For more information, see section 171 and Pub. 550.

If you claim a bond premium deduction for the estate or trust, figure the deduction on a separate sheet and attach it to Form 1041.

**Casualty and theft losses.** Use **Form 4684**, Casualties and Thefts, to figure any deductible casualty and theft losses.

**Deduction for clean-fuel vehicles.** Section 179A allows a deduction for part of the cost of qualified clean-fuel vehicle property. See **Pub. 535**, Business Expenses, for more details.

**Net operating loss deduction (NOLD).** An estate or trust is allowed the net



operating loss deduction (NOLD) under section 172.

If you claim an NOLD for the estate or trust, figure the deduction on a separate sheet and attach it to this return.

**Estate's or trust's share of amortization, depreciation, and depletion not claimed elsewhere.** If you cannot deduct the amortization, depreciation, and depletion as rent or royalty expenses on Schedule E (Form 1040), or as business or farm expenses on Schedule C, C-EZ, or F (Form 1040), itemize the fiduciary's share of the deductions on an attached sheet and include them on line 15a. Itemize each beneficiary's share of the deductions and report them on the appropriate line of Schedule K-1 (Form 1041).

**Commercial revitalization deduction.** An estate or trust may qualify for a deduction if it constructs, purchases, or substantially rehabilitates a qualified building in a renewal community. See section 1400I for details.

### Line 15b—Allowable Miscellaneous Itemized Deductions Subject to the 2% Floor

Miscellaneous itemized deductions are deductible only to the extent that the aggregate amount of such deductions exceeds 2% of adjusted gross income (AGI).

Among the miscellaneous itemized deductions that must be included on line 15b are expenses for the production or collection of income under section 212, such as investment advisory fees, subscriptions to investment advisory publications, and the cost of safe deposit boxes.

Miscellaneous itemized deductions **do not** include deductions for:

- Interest under section 163.
- Taxes under section 164.
- The amortization of bond premium under section 171.
- Estate taxes attributable to income in respect of a decedent under section 691(c).
- Expenses paid or incurred in connection with the administration of the estate or trust that would not have been incurred if the property were **not** held in the estate or trust.

For other exceptions, see section 67(b).

**How to figure AGI for estates and trusts.** You figure AGI by subtracting the following from total income on line 9 of page 1:

1. The administration costs of the estate or trust (the total of lines 12, 14, and 15a to the extent they are costs incurred in the administration of the estate or trust) that would not have been incurred if the property were **not** held by the estate or trust;

2. The income distribution deduction (line 18);

3. The amount of the exemption (line 20);

4. The deduction for clean-fuel vehicles claimed on line 15a; and

5. The net operating loss deduction claimed on line 15a.

For those estates and trusts whose income distribution deduction is limited to the actual distribution, and **not** the DNI (i.e., the income distribution is less than the DNI), when computing the AGI, use the amount of the actual distribution.

For those estates and trusts whose income distribution deduction is limited to the DNI (i.e., the actual distribution exceeds the DNI), the DNI must be figured taking into account the allowable miscellaneous itemized deductions (AMID) after application of the 2% floor. In this situation there are two unknown amounts: **(a)** the AMID; and **(b)** the DNI.

**Computing line 15b.** To compute line 15b, use the equation below:

$$\text{AMID} = \text{Total miscellaneous itemized deductions} - (.02(\text{AGI}))$$

The following example illustrates how algebraic equations can be used to solve for these unknown amounts.

**Example.** The Malcolm Smith Trust, a complex trust, earned \$20,000 of dividend income, \$20,000 of capital gains, and a fully deductible \$5,000 loss from XYZ partnership (chargeable to corpus) in 2003. The trust instrument provides that capital gains are added to corpus. 50% of the fiduciary fees are allocated to income and 50% to corpus. The trust claimed a \$2,000 deduction on line 12 of Form 1041. The trust incurred \$1,500 of miscellaneous itemized deductions (chargeable to income), which are subject to the 2% floor. There are no other deductions. The trustee made a discretionary distribution of the accounting income of \$17,500 to the trust's sole beneficiary.

Because the actual distribution can reasonably be expected to exceed the DNI, the trust must figure the DNI, taking into account the allowable miscellaneous itemized deductions, to determine the amount to enter on line 15b.

The trust also claims an exemption of \$100 on line 20.

Using the facts in this example:

$$\text{AMID} = 1,500 - (.02(\text{AGI}))$$

In all situations, use the following equation to compute the AGI:

$\text{AGI} = (\text{line } 9) - (\text{the total of lines } 12, 14, \text{ and } 15a \text{ to the extent they are costs incurred in the administration of the estate or trust that would not have been incurred if the property were not held by the estate or trust}) - (\text{line } 18) - (\text{line } 20).$

**Note:** *There are no other deductions claimed by the trust on line 15a that are deductible in arriving at AGI.*

Figuring AGI in this example, we get:

$$\text{AGI} = 35,000 - 2,000 - \text{DNI} - 100$$

Since the value of line 18 is not known because it is limited to the DNI, you are left with the following:

$$\text{AGI} = 32,900 - \text{DNI}$$

Substitute the value of AGI in the equation:

$$\text{AMID} = 1,500 - (.02(32,900 - \text{DNI}))$$

The equation cannot be solved until the value of DNI is known. The DNI can be expressed in terms of the AMID. To do this, compute the DNI using the known values. In this example, the DNI is equal to the total income of the trust (less any capital gains allocated to corpus; or plus any capital loss from line 4); less total deductions from line 16 (excluding any miscellaneous itemized deductions); less the AMID.

Thus,  $\text{DNI} = (\text{line } 9) - (\text{line } 16a, \text{ column } (2) \text{ of Schedule D (Form 1041)}) - (\text{line } 16) - (\text{AMID})$

Substitute the known values:

$$\text{DNI} = 35,000 - 20,000 - 2,000 - \text{AMID}$$

$$\text{DNI} = 13,000 - \text{AMID}$$

Substitute the value of DNI in the equation to solve for AMID:

$$\text{AMID} = 1,500 - (.02(32,900 - (13,000 - \text{AMID})))$$

$$\text{AMID} = 1,500 - (.02(32,900 - 13,000 + \text{AMID}))$$

$$\text{AMID} = 1,500 - (658 - 260 + .02\text{AMID})$$

$$\text{AMID} = 1,102 - .02\text{AMID}$$

$$1.02\text{AMID} = 1,102$$

$$\text{AMID} = 1,080$$

$$\text{DNI} = 11,920 \text{ (i.e., } 13,000 - 1,080)$$

$$\text{AGI} = 20,980 \text{ (i.e., } 32,900 - 11,920)$$

**Note:** *The income distribution deduction is equal to the smaller of the distribution (\$17,500) or the DNI (\$11,920).*

Enter the value of AMID on line 15b (the DNI should equal line 7 of Schedule B) and complete the rest of Form 1041 according to the instructions.

If the 2% floor is more than the deductions subject to the 2% floor, no deductions are allowed.

### Line 18—Income Distribution Deduction

If the estate or trust was required to distribute income currently or if it paid, credited, or was required to distribute any other amounts to beneficiaries during the tax year, complete Schedule B to determine the estate's or trust's income distribution deduction. However, if you are filing for a pooled income fund, do not complete Schedule B. Instead, attach a statement to support the computation of the income distribution deduction. If the estate or trust claims an income distribution deduction, complete and attach:

- Part I (through line 9) and Part II of Schedule I to refigure the deduction on a minimum tax basis **and**

- Schedule K-1 (Form 1041) for each beneficiary to which a distribution was made or required to be made.

**Cemetery perpetual care fund.** On line 18, deduct the amount, not more than \$5 per gravesite, paid for maintenance of cemetery property. To the right of the entry space for line 18, enter the number of gravesites. Also write "Section 642(i) trust" in parentheses after the trust's name at the top of Form 1041. You do not have to complete Schedules B of Form 1041 and K-1 (Form 1041).

Do not enter less than zero on line 18.

**Line 19—Estate Tax Deduction (Including Certain Generation-Skipping Transfer Taxes)**

If the estate or trust includes income in respect of a decedent (IRD) in its gross income, and such amount was included in the decedent's gross estate for estate tax purposes, the estate or trust is allowed to deduct in the same tax year that the income is included, that portion of the estate tax imposed on the decedent's estate that is attributable to the inclusion of the IRD in the decedent's estate. For an example of the computation, see Regulations section 1.691(c)-1 and Pub. 559.

If any amount properly paid, credited, or required to be distributed by an estate or trust to a beneficiary consists of IRD received by the estate or trust, do not include such amounts in determining the estate tax deduction for the estate or trust. Figure the deduction on a separate sheet. Attach the sheet to your return.



*If you claim a deduction for estate tax attributable to qualified dividends or capital gains, you may have to adjust the amount on Form 1041, page 1, line 2b(2), or Schedule D, line 19.*

Also, a deduction is allowed for the GST tax imposed as a result of a taxable termination or a direct skip occurring as a result of the death of the transferor. See section 691(c)(3). Enter the estate's or trust's share of these deductions on line 19.

**Line 20—Exemption**

**Decedents' estates.** A decedent's estate is allowed a \$600 exemption.

**Trusts required to distribute all income currently.** A trust whose governing instrument requires that all income be distributed currently is allowed a \$300 exemption, even if it distributed amounts other than income during the tax year.

**Qualified disability trusts.** A qualified disability trust is allowed a \$3,050 exemption if the trust's modified AGI is less than or equal to \$139,500. If its modified AGI exceeds \$139,500, complete the worksheet on page 18 to figure the amount of the trust's exemption. To figure modified AGI, follow the instructions for figuring AGI for line 15b on page 17, **except** use zero as the amount of the trust's exemption when figuring AGI.

A **qualified disability trust** is any trust:

1. Described in 42 U.S.C. 1396p(c)(2)(B)(iv) and established solely for the benefit of an individual under 65 years of age who is disabled and
2. All of the beneficiaries of which are determined by the Commissioner of Social Security to have been disabled for some part of the tax year within the meaning of 42 U.S.C. 1382c(a)(3).

A trust will not fail to meet **2** above just because the trust's corpus may revert to a person who is not disabled after the trust ceases to have any disabled beneficiaries.

**All other trusts.** A trust not described above is allowed a \$100 exemption.

**Tax and Payments**

**Line 22—Taxable Income**

**Net operating loss.** If line 22 is a loss, the estate or trust may have a net operating loss (NOL). Do not include the deductions claimed on lines 13, 18, and 20 when figuring the amount of the NOL.

Generally, an NOL may be carried back to the prior 2 tax years (3 years to the extent the loss is an eligible loss; 5 years to the extent the loss is a farming loss; 10 years to the extent the loss is a specified liability loss). An estate or trust may also elect to carry an NOL forward only, instead of first carrying it back. For more information, see the Instructions for Form 1045.

Complete Schedule A of **Form 1045**, Application for Tentative Refund, to figure the amount of the NOL that is available for carryback or carryover. Use Form 1045 or file an amended return to apply for a refund based on an NOL carryback. For more details, see **Pub. 536**, Net Operating Losses (NOLs) for Individuals, Estates, and Trusts.

On the termination of the estate or trust, any unused NOL carryover that would be allowable to the estate or trust in a later tax year, but for the termination, is allowed to the beneficiaries succeeding to the property of the estate or trust. See the instructions for Schedule K-1, lines 13d and 13e.

**Excess deductions on termination.** If the estate or trust has for its final year deductions (excluding the charitable deduction and exemption) in excess of its gross income, the excess is allowed as an itemized deduction to the beneficiaries succeeding to the property of the estate or trust.

**Exemption Worksheet for Qualified Disability Trusts Only—Line 20**

*Keep for Your Records*

**Note:** If the trust's modified AGI\* is less than or equal to \$139,500, enter \$3,050 on Form 1041, line 20. Otherwise, complete the worksheet below to figure the trust's exemption.



|  |    |           |
|--|----|-----------|
| 1. Maximum exemption . . . . .   | 1. | \$3,050   |
| 2. Enter the trust's modified AGI* . . . . .   | 2. | _____     |
| 3. Threshold amount . . . . .  | 3. | \$139,500 |
| 4. Subtract line 3 from line 2 . . . . .   | 4. | _____     |
| <b>Note:</b> If line 4 is more than \$122,500, stop here. <b>The trust's exemption is zero.</b>  |    |           |
| 5. Divide line 4 by \$2,500. If result is not a whole number, increase it to the next higher whole number (e.g., increase 0.0004 to 1) . . . . . | 5. | _____     |
| 6. Multiply line 5 by 2% (.02) and enter the result as a decimal . . . . .   | 6. | _____     |
| 7. Multiply line 1 by line 6 . . . . .   | 7. | _____     |
| 8. <b>Exemption.</b> Subtract line 7 from line 1. Enter the result here and on Form 1041, line 20 . . . . .                                      | 8. | _____     |

\*Figure the trust's modified AGI in the same manner as AGI is figured in the line 15b instructions on page 17, **except** use zero when figuring the amount of the trust's exemption.

In general, an unused NOL carryover that is allowed to beneficiaries (as explained above) cannot also be treated as an excess deduction. However, if the final year of the estate or trust is also the last year of the NOL carryover period, the NOL carryover not absorbed in that tax year by the estate or trust is included as an excess deduction. See the instructions for Schedule K-1, line 13a.

### Line 24a—2003 Estimated Tax Payments and Amount Applied From 2002 Return

Enter the amount of any estimated tax payment you made with Form 1041-ES for 2003 plus the amount of any overpayment from the 2002 return that was applied to the 2003 estimated tax.

If the estate or trust is the beneficiary of another trust and received a payment of estimated tax that was credited to the trust (as reflected on the Schedule K-1 issued to the trust), then report this amount separately with the notation "section 643(g)" in the space next to line 24a.



*Do not include on Form 1041 estimated tax paid by an individual before death. Instead, include the payments on the decedent's final income tax return.*

### Line 24b—Estimated Tax Payments Allocated to Beneficiaries

The trustee (or executor, for the final year of the estate) may elect under section 643(g) to have any portion of its estimated tax treated as a payment of estimated tax made by a beneficiary or beneficiaries. The election is made on **Form 1041-T**, Allocation of Estimated Tax Payments to Beneficiaries, which must be filed by the 65th day after the close of the trust's tax year. Form 1041-T shows the amounts to be allocated to each beneficiary. This amount is reported on the beneficiary's Schedule K-1, line 14a.

Attach Form 1041-T to your return **only** if you have not yet filed it; however, attaching Form 1041-T to Form 1041 does **not** extend the due date for filing Form 1041-T. If you have already filed Form 1041-T, do not attach a copy to your return.



*Failure to file Form 1041-T by the due date (March 5, 2004, for calendar year estates and trusts) will result in an invalid election. An invalid election will require the filing of amended Schedules K-1 for each beneficiary who was allocated a payment of estimated tax.*

### Line 24d—Tax Paid With Extension of Time To File

If you filed either Form 2758 (for estates only), Form 8736, or Form 8800 to request an extension of time to file Form 1041, enter the amount that you paid with the extension request and check the appropriate box(es).

### Line 24e—Federal Income Tax Withheld

Use line 24e to claim a credit for any Federal income tax withheld (and not repaid) by: **(a)** an employer on wages and salaries of a decedent received by the decedent's estate; **(b)** a payer of certain gambling winnings (e.g., state lottery winnings); or **(c)** a payer of distributions from pensions, annuities, retirement or profit-sharing plans, IRAs, insurance contracts, etc., received by a decedent's estate or trust. Attach a copy of **Form W-2, Form W-2G, or Form 1099-R** to the front of the return.



*Except for backup withholding (as explained below), withheld income tax may not be passed through to beneficiaries on either Schedule K-1 or Form 1041-T.*

**Backup withholding.** If the estate or trust received a 2003 Form 1099 showing Federal income tax withheld (i.e., backup withholding) on interest income, dividends, or other income, check the box and include the amount withheld on income retained by the estate or trust in the total for line 24e.

Report on Schedule K-1 (Form 1041), line 14, any credit for backup withholding on income distributed to the beneficiary.

### Line 24f—Credit For Tax Paid on Undistributed Capital Gains

Attach Copy B of **Form 2439**, Notice to Shareholder of Undistributed Long-Term Capital Gains.

### Line 24g—Credit for Federal Tax on Fuels

Enter any credit for Federal excise taxes paid on fuels that are ultimately used for nontaxable purposes (e.g., an off-highway business use). Attach **Form 4136**, Credit for Federal Tax Paid on Fuels. See **Pub. 378**, Fuel Tax Credits and Refunds, for more information.

### Line 26—Estimated Tax Penalty

If line 27 is at least \$1,000 and more than 10% of the tax shown on Form 1041, or the estate or trust underpaid its 2003 estimated tax liability for any payment period, it may owe a penalty. See Form 2210 to determine whether the estate or trust owes a penalty and to figure the amount of the penalty.

**Note:** *The penalty may be waived under certain conditions. See **Pub. 505**, Tax Withholding and Estimated Tax, for details.*

### Line 27—Tax Due

You must pay the tax in full when the return is filed. Make the check or money order payable to the "United States Treasury." Write the EIN and "2003 Form 1041" on the payment. Enclose, but do not attach, the payment with Form 1041.



*You may use EFTPS to pay the tax due for a trust. See **Electronic Deposits** on page 8.*

### Line 29a—Credited to 2004 Estimated Tax

Enter the amount from line 28 that you want applied to the estate's or trust's 2004 estimated tax.

## Schedule A—Charitable Deduction

### General Instructions

Generally, any part of the gross income of an estate or trust (other than a simple trust) that, under the terms of the will or governing instrument, is paid (or treated as paid) during the tax year for a charitable purpose specified in section 170(c) is allowed as a deduction to the estate or trust. It is not necessary that the charitable organization be created or organized in the United States.

A pooled income fund, a nonexempt charitable trust treated as a private foundation, or a trust with unrelated business income should attach a separate sheet to Form 1041 instead of using Schedule A of Form 1041 to figure the charitable deduction.

**Additional return to be filed by trusts.** Trusts that claim a charitable deduction must also file Form 1041-A. See Form 1041-A for exceptions.

**Election to treat contributions as paid in the prior tax year.** The fiduciary of an estate or trust may elect to treat as paid during the tax year any amount of gross income received during that tax year or any prior tax year that was paid in the next tax year for a charitable purpose.

For example, if a calendar year estate or trust makes a qualified charitable contribution on February 7, 2004, from income earned in 2003 or prior, then the fiduciary can elect to treat the contribution as paid in 2003.

To make the election, the fiduciary must file a statement with Form 1041 for the tax year in which the contribution is treated as paid. This statement must include:

1. The name and address of the fiduciary;
2. The name of the estate or trust;
3. An indication that the fiduciary is making an election under section 642(c)(1) for contributions treated as paid during such tax year;
4. The name and address of each organization to which any such contribution is paid; and
5. The amount of each contribution and date of actual payment or, if applicable, the total amount of contributions paid to each organization during the next tax year, to be treated as paid in the prior tax year.

The election must be filed by the due date (including extensions) for Form 1041 for the next tax year. If the original return was filed on time, you may make the election on an amended return filed no

later than 6 months after the due date of the return (excluding extensions). Write "Filed pursuant to section 301.9100-2" at the top of the amended return and file it at the same address you used for your original return.

For more information about the charitable deduction, see section 642(c) and related regulations.

## Specific Instructions

### Line 1—Amounts Paid or Permanently Set Aside for Charitable Purposes From Gross Income

Enter amounts that were paid for a charitable purpose out of the estate's or trust's gross income, including any capital gains that are attributable to income under the governing instrument or local law. Include amounts paid during the tax year from gross income received in a prior tax year, but only if no deduction was allowed for any prior tax year for these amounts.

Estates, and certain trusts, may claim a deduction for amounts permanently set aside for a charitable purpose from gross income. Such amounts must be permanently set aside during the tax year to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, or for the establishment, acquisition, maintenance, or operation of a public cemetery not operated for profit.

For a trust to qualify, the trust may not be a simple trust, and the set aside amounts must be required by the terms of a trust instrument that was created on or before October 9, 1969.

Further, the trust instrument must provide for an irrevocable remainder interest to be transferred to or for the use of an organization described in section 170(c); or the trust must have been created by a grantor who was at all times after October 9, 1969, under a mental disability to change the terms of the trust.

Also, certain testamentary trusts that were established by a will that was executed on or before October 9, 1969, may qualify. See Regulations section 1.642(c)-2(b).

Do not include any capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes. Instead, enter these amounts on line 4.

### Line 2—Tax-Exempt Income Allocable to Charitable Contributions

Any estate or trust that pays or sets aside any part of its income for a charitable purpose must reduce the deduction by the portion allocable to any tax-exempt income. If the governing instrument specifically provides as to the source from which amounts are paid, permanently set aside, or to be used for charitable

purposes, the specific provisions control. In all other cases, determine the amount of tax-exempt income allocable to charitable contributions by multiplying line 1 by a fraction, the numerator of which is the total tax-exempt income of the estate or trust, and the denominator of which is the gross income of the estate or trust. Do not include in the denominator any losses allocated to corpus.

### Line 4—Capital Gains for the Tax Year Allocated to Corpus and Paid or Permanently Set Aside for Charitable Purposes

Enter the total of all capital gains for the tax year that are:

- Allocated to corpus and
- Paid or permanently set aside for charitable purposes.

### Line 6—Section 1202 Exclusion Allocable to Capital Gains Paid or Permanently Set Aside for Charitable Purposes

If the exclusion of gain from the sale or exchange of qualified small business stock was claimed, enter the part of the gain included on Schedule A, lines 1 and 4, that was excluded under section 1202.

## Schedule B—Income Distribution Deduction

### General Instructions

If the estate or trust was required to distribute income currently or if it paid, credited, or was required to distribute any other amounts to beneficiaries during the tax year, complete Schedule B to determine the estate's or trust's income distribution deduction.

**Note:** Use Schedule I to compute the DNI and income distribution deduction on a minimum tax basis.

**Pooled income funds.** Do not complete Schedule B for these funds. Instead, attach a separate statement to support the computation of the income distribution deduction. See **Pooled Income Funds** on page 6 for more information.

**Separate share rule.** If a single trust or an estate has more than one beneficiary, and if different beneficiaries have substantially separate and independent shares, their shares are treated as separate trusts or estates for the sole purpose of determining the DNI allocable to the respective beneficiaries.

If the separate share rule applies, figure the DNI allocable to each beneficiary on a separate sheet and attach the sheet to this return. Any deduction or loss that is applicable solely to one separate share of the trust or estate is not available to any other share of the same trust or estate.

For more information, see section 663(c) and related regulations.

**Withholding of tax on foreign persons.** The fiduciary may be liable for withholding

tax on distributions to beneficiaries who are foreign persons. For more information, see **Pub. 515**, Withholding of Tax on Nonresident Aliens and Foreign Entities, and Forms 1042 and 1042-S.

## Specific Instructions

### Line 1—Adjusted Total Income

Generally, enter on line 1, Schedule B, the amount from line 17 on page 1 of Form 1041. However, if **both** line 4 and line 17 on page 1 of Form 1041 are losses, enter on line 1, Schedule B, the **smaller** of those losses. If line 4 is zero or a gain and line 17 is a loss, enter zero on line 1, Schedule B.

If you are filing for a simple trust, subtract from adjusted total income any extraordinary dividends or taxable stock dividends included on page 1, line 2, and determined under the governing instrument and applicable local law to be allocable to corpus.

### Line 2—Adjusted Tax-Exempt Interest

To figure the adjusted tax-exempt interest:

**Step 1.** Add tax-exempt interest income on line 2 of Schedule A, any expenses allowable under section 212 allocable to tax-exempt interest, and any interest expense allocable to tax-exempt interest.

**Step 2.** Subtract the Step 1 total from the amount of tax-exempt interest (including exempt-interest dividends) received.

Section 212 expenses that are directly allocable to tax-exempt interest are allocated only to tax-exempt interest. A reasonable proportion of section 212 expenses that are indirectly allocable to both tax-exempt interest and other income must be allocated to each class of income.

Figure the interest expense allocable to tax-exempt interest according to the guidelines in Rev. Proc. 72-18, 1972-1 C.B. 740.

See Regulations sections 1.643(a)-5 and 1.265-1 for more information.

### Line 3

Include all capital gains, whether or not distributed, that are attributable to income under the governing instrument or local law. For example, if the trustee distributed 50% of the current year's capital gains to the income beneficiaries (and reflects this amount in column (1), line 16a of Schedule D (Form 1041)), but under the governing instrument all capital gains are attributable to income, then include 100% of the capital gains on line 3. If the amount on Schedule D (Form 1041), line 16a, column (1) is a net loss, enter zero.

If the exclusion of gain from the sale or exchange of qualified small business stock was claimed, **do not** reduce the gain on line 3 by any amount excluded under section 1202.

## Line 5

In figuring the amount of long-term and short-term capital gain for the tax year included on Schedule A, line 1, the specific provisions of the governing instrument control if the instrument specifically provides as to the source from which amounts are paid, permanently set aside, or to be used for charitable purposes.

In all other cases, determine the amount to enter by multiplying line 1 of Schedule A by a fraction, the numerator of which is the amount of net capital gains that are included in the accounting income of the estate or trust (i.e., not allocated to corpus) and are distributed to charities, and the denominator of which is all items of income (including the amount of such net capital gains) included in the DNI.

Reduce the amount on line 5 by any allocable section 1202 exclusion.

## Line 8—Accounting Income

If you are filing for a decedent's estate or a simple trust, skip this line. If you are filing for a complex trust, enter the income for the tax year determined under the terms of the governing instrument and applicable local law. Do not include extraordinary dividends or taxable stock dividends determined under the governing instrument and applicable local law to be allocable to corpus.

## Lines 9 and 10

Do not include any:

- Amounts deducted on prior year's return that were required to be distributed in the prior year.
- Amount that is properly paid or credited as a gift or bequest of a specific amount of money or specific property. (To qualify as a gift or bequest, the amount must be paid in three or fewer installments.) An amount that can be paid or credited only from income is not considered a gift or bequest.
- Amount paid or permanently set aside for charitable purposes or otherwise qualifying for the charitable deduction.

## Line 9—Income Required To Be Distributed Currently

Line 9 is to be completed by all simple trusts as well as complex trusts and decedent's estates, that are required to distribute income currently, whether it is distributed or not. The determination of whether trust income is required to be distributed currently depends on the terms of the governing instrument and the applicable local law.

The line 9 distributions are referred to as first tier distributions and are deductible by the estate or trust to the extent of the DNI. The beneficiary includes such amounts in his or her income to the extent of his or her proportionate share of the DNI.

## Line 10—Other Amounts Paid, Credited, or Otherwise Required To Be Distributed

Line 10 is to be completed **only** by a decedent's estate or complex trust. These distributions consist of any other amounts paid, credited, or required to be distributed and are referred to as second tier distributions. Such amounts include annuities to the extent not paid out of income, mandatory and discretionary distributions of corpus, and distributions of property in kind.

If Form 1041-T was timely filed to elect to treat estimated tax payments as made by a beneficiary, the payments are treated as paid or credited to the beneficiary on the last day of the tax year and must be included on line 10.

Unless a section 643(e)(3) election is made, the value of all noncash property actually paid, credited, or required to be distributed to any beneficiaries is the smaller of:

1. The estate's or trust's adjusted basis in the property immediately before distribution, plus any gain or minus any loss recognized by the estate or trust on the distribution (basis of beneficiary) or
2. The fair market value (FMV) of such property.

If a section 643(e)(3) election is made by the fiduciary, then the amount entered on line 10 will be the FMV of the property.

A fiduciary of a complex trust or a decedent's estate may elect to treat any amount paid or credited to a beneficiary within 65 days following the close of the tax year as being paid or credited on the last day of that tax year. To make this election, see the instructions for Question 6 on page 24.

The beneficiary includes the amounts on line 10 in his or her income only to the extent of his or her proportionate share of the DNI.

**Complex trusts.** If the second tier distributions exceed the DNI allocable to the second tier, the trust may have an accumulation distribution. See the line 11 instructions below.

## Line 11—Total Distributions

If line 11 is more than line 8, and you are filing for a complex trust that has previously accumulated income, see the instructions on page 38 to see if you must complete **Schedule J (Form 1041)**.

## Line 12—Adjustment for Tax-Exempt Income

In figuring the income distribution deduction, the estate or trust is not allowed a deduction for any item of the DNI that is not included in the gross income of the estate or trust. Thus, for purposes of figuring the allowable income distribution deduction, the DNI (line 7) is figured without regard to any tax-exempt interest.

If tax-exempt interest is the only tax-exempt income included in the total

distributions (line 11), and the DNI (line 7) is less than or equal to line 11, then enter on line 12 the amount from line 2.

If tax-exempt interest is the only tax-exempt income included in the total distributions (line 11), and the DNI is more than line 11 (i.e., the estate or trust made a distribution that is less than the DNI), then figure the adjustment by multiplying line 2 by a fraction, the numerator of which is the total distributions (line 11), and the denominator of which is the DNI (line 7). Enter the result on line 12.

If line 11 includes tax-exempt income other than tax-exempt interest, figure line 12 by subtracting the total of the following from tax-exempt income included on line 11:

1. The charitable contribution deduction allocable to such tax-exempt income and
2. Expenses allocable to tax-exempt income.

Expenses that are directly allocable to tax-exempt income are allocated only to tax-exempt income. A reasonable proportion of expenses indirectly allocable to both tax-exempt income and other income must be allocated to each class of income.

## Schedule G—Tax Computation

### Line 1a

**2003 tax rate schedule.** For tax years beginning in 2003, figure the tax using the Tax Rate Schedule below and enter the tax on line 1a. However, see the instructions for **Schedule D** and the **Qualified Dividends Tax Worksheet** below.

2003 Tax Rate Schedule

| If taxable income is: |                |                |                      |
|-----------------------|----------------|----------------|----------------------|
| Over —                | But not over — | Its tax is:    | Of the amount over — |
| \$0                   | \$1,900        | 15%            | \$0                  |
| 1,900                 | 4,500          | \$285.00 + 25% | 1,900                |
| 4,500                 | 6,850          | 935.00 + 28%   | 4,500                |
| 6,850                 | 9,350          | 1,593.00 + 33% | 6,850                |
| 9,350                 | -----          | 2,418.00 + 35% | 9,350                |

**Schedule D and Schedule D Tax Worksheet.** Use Part V of Schedule D or the Schedule D Tax Worksheet, whichever is applicable, to figure the estate's or trust's tax if the estate or trust files Schedule D and has:

- A net capital gain and any taxable income or
- Qualified dividends on line 2b(2) of Form 1041 and any taxable income.

**Qualified Dividends Tax Worksheet.** If you do not have to complete Part I or Part II of Schedule D and the estate or trust has an amount entered on line 2b(2) of

Form 1041 and any taxable income (line 22), then figure the estate's or trust's tax using the worksheet below and enter the tax on line 1a.

**Line 2a—Foreign Tax Credit**

Attach **Form 1116**, Foreign Tax Credit (Individual, Estate, Trust, or Nonresident Alien Individual), if you elect to claim credit for income or profits taxes paid or accrued to a foreign country or a U.S. possession. The estate or trust may claim credit for that part of the foreign taxes not allocable to the beneficiaries (including charitable beneficiaries). Enter the estate's or trust's share of the credit on line 2a. See **Pub. 514**, Foreign Tax Credit for Individuals, for details.

**Line 2b—Other Nonbusiness Credits**

**Nonconventional source fuel credit.** If the estate or trust claims any section 29 credit for producing fuel from a nonconventional source, figure the credit on a separate sheet and attach it to the return. Include the credit on line 2b.

**Qualified electric vehicle credit.** Complete and attach **Form 8834**, Qualified Electric Vehicle Credit, if the estate or trust claims a credit for the purchase of a new qualified electric vehicle. Include the credit on line 2b.

**Line 2c—General Business Credit**

Complete this line if the estate or trust is claiming any of the credits listed below. Use the appropriate credit form to figure the credit. If the estate or trust does not have to file **Form 3800**, General Business Credit, enter the form number and the

amount of the credit in the space provided.

The estate or trust must file **Form 3800** if any of the following apply.

1. The estate or trust has more than one of the credits listed below (other than the empowerment zone and renewal community employment credit or the New York Liberty Zone business employee credit).
2. The estate or trust has general credits from an electing large partnership shown in box 7 of Schedule K-1 (Form 1065-B).
3. The estate or trust has a carryback or carryforward of any of these credits (other than the empowerment zone and renewal community employment credit or the New York Liberty Zone business employee credit).
4. Any of these credits (other than the low-income housing credit, the empowerment zone and renewal community employment credit, or the New York Liberty Zone business employee credit) is from a passive activity.

Enter the amount from **Form 3800** on line 2c. Also, be sure to check the box for **Form 3800**.

Do not include any amounts that are allocated to a beneficiary. Credits that are allocated between the estate or trust and the beneficiaries are listed in the instructions for Schedule K-1, line 14, on page 41. Generally, these credits are apportioned on the basis of the income allocable to the estate or trust and the beneficiaries. Report the estate's or trust's share of the following general business credits on Schedule G, line 2c.

- Investment credit (Form 3468).
- Work opportunity credit (Form 5884).
- Welfare-to-work credit (Form 8861).
- Credit for alcohol used as fuel (Form 6478).
- Credit for increasing research activities (Form 6765).
- Low-income housing credit (Form 8586).
- Enhanced oil recovery credit (Form 8830).
- Disabled access credit (Form 8826).
- Renewable electricity production credit (Form 8835).
- Empowerment zone and renewal community employment credit (Form 8844).
- Indian employment credit (Form 8845).
- Credit for employer social security and Medicare taxes paid on certain employee tips (Form 8846).
- Orphan drug credit (Form 8820).
- New markets credit (Form 8874).
- Credit for small employer pension plan startup costs (Form 8881).
- Credit for employer-provided child care facilities and services (Form 8882).
- New York Liberty Zone business employee credit (Form 8884).
- Credit for contributions to selected community development corporations (Form 8847).
- General credits from an electing large partnership. Report these credits on Form 3800, line 1r.

**Line 2d—Credit for Prior Year Minimum Tax**

An estate or trust that paid alternative minimum tax in a previous year may be eligible for a minimum tax credit in 2003. See **Form 8801**, Credit for Prior Year

**Qualified Dividends Tax Worksheet—Schedule G, line 1a**

*Keep for Your Records*

**Caution:** Do not use this worksheet if the estate or trust must complete Schedule D.



|   |     |       |
|---|-----|-------|
| 1. Enter the amount from Form 1041, line 22   | 1.  | _____ |
| 2. Enter the amount from Form 1041, line 2b(2)  | 2.  | _____ |
| 3. If you are claiming investment interest expense on Form 4952, enter the amount from line 4g; otherwise enter -0- | 3.  | _____ |
| 4. Subtract line 3 from line 2. If zero or less, enter -0-  | 4.  | _____ |
| 5. Subtract line 4 from line 1. If zero or less, enter -0-  | 5.  | _____ |
| 6. Enter the <b>smaller</b> of the amount on line 1 or \$1,900  | 6.  | _____ |
| 7. Is the amount on line 5 equal to or more than the amount on line 6?  |     |       |
| <input type="checkbox"/> <b>Yes.</b> Skip lines 7 through 9; go to line 10 and check the "No" box.                  |     |       |
| <input type="checkbox"/> <b>No.</b> Enter the amount from line 5  | 7.  | _____ |
| 8. Subtract line 7 from line 6  | 8.  | _____ |
| 9. Multiply line 8 by 5% (.05)  | 9.  | _____ |
| 10. Are the amounts on lines 4 and 8 the same?  |     |       |
| <input type="checkbox"/> <b>Yes.</b> Skip lines 10 through 13; go to line 14.                                       |     |       |
| <input type="checkbox"/> <b>No.</b> Enter the <b>smaller</b> of line 1 or line 4                                    | 10. | _____ |
| 11. Enter the amount from line 8 (if line 8 is blank, enter -0-)  | 11. | _____ |
| 12. Subtract line 11 from line 10   | 12. | _____ |
| 13. Multiply line 12 by 15% (.15)   | 13. | _____ |
| 14. Figure the tax on the amount on line 5. Use the 2003 Tax Rate Schedule  | 14. | _____ |
| 15. Add lines 9, 13, and 14   | 15. | _____ |
| 16. Figure the tax on the amount on line 1. Use the 2003 Tax Rate Schedule  | 16. | _____ |
| 17. <b>Tax on all taxable income.</b> Enter the <b>smaller</b> of line 15 or line 16 here and on Sch. G, line 1a    | 17. | _____ |

Minimum Tax—Individuals, Estates, and Trusts.

### Line 3—Total Credits

If the estate or trust received a qualified zone academy bond credit as a shareholder in an S corporation, include the credit in the line 3 total. To figure the amount of the allowable credit, the estate or trust must complete **Form 8860, Qualified Zone Academy Bond Credit**. On the dotted line to the left of the entry, write “QZAB” and the amount of the credit.

### Line 5—Recapture Taxes

**Recapture of investment credit.** If the estate or trust disposed of investment credit property or changed its use before the end of the recapture period, see **Form 4255, Recapture of Investment Credit**, to figure the recapture tax allocable to the estate or trust.

**Recapture of low-income housing credit.** If the estate or trust disposed of property (or there was a reduction in the qualified basis of the property) on which the low-income housing credit was claimed, see **Form 8611, Recapture of Low-Income Housing Credit**, to figure any recapture tax allocable to the estate or trust.

**Recapture of qualified electric vehicle credit.** If the estate or trust claimed the qualified electric vehicle credit in a prior tax year for a vehicle that ceased to qualify for the credit, part or all of the credit may have to be recaptured. See Pub. 535 for details. If the estate or trust owes any recapture tax, include it on line 5 and write “QEVCR” on the dotted line to the left of the entry space.

**Recapture of the Indian employment credit.** Generally, if the estate or trust terminates a qualified employee less than 1 year after the date of initial employment, any Indian employment credit allowed for a prior tax year by reason of wages paid or incurred to that employee must be recaptured. See Form 8845 for details. If the estate or trust owes any recapture tax, include it on line 5 and write “IECR” on the dotted line to the left of the entry space.

**Recapture of the new markets credit.** If the estate or trust owes any new markets recapture tax, include it on line 5 and write “NMCR” on the dotted line to the left of the entry space. For more information, including how to figure the recapture amount, see section 45D(g).

**Recapture of the credit for employer-provided child care facilities.** If the facility ceased to operate as a qualified child care facility or there was a change in ownership, part or all of the credit may have to be recaptured. See Form 8882 for details. If the estate or trust owes any recapture tax, include it on line 5 and write “ECCFR” on the dotted line to the left of the entry space.

### Line 6—Household Employment Taxes

If any of the following apply, get **Schedule H (Form 1040)**, Household Employment Taxes, and its instructions, to see if the estate or trust owes these taxes.

1. The estate or trust paid **any one** household employee cash wages of \$1,400 or more in 2003. Cash wages include wages paid by checks, money orders, etc. When figuring the amount of cash wages paid, combine cash wages paid by the estate or trust with cash wages paid to the household employee in the same calendar year by the household of the decedent or beneficiary for whom the administrator, executor, or trustee of the estate or trust is acting.

2. The estate or trust withheld Federal income tax during 2003 at the request of any household employee.

3. The estate or trust paid **total** cash wages of \$1,000 or more in **any** calendar quarter of 2002 or 2003 to household employees.

### Line 7—Total Tax

**Tax on electing small business trusts (ESBTs).** Attach the tax computation to the return. To the left of the line 7 entry space, write “Sec. 641(c)” and the amount of tax on the S corporation items. Include this amount in the total tax on line 7.

See **Electing Small Business Trusts** on page 7 for the special tax computation rules that apply to the portion of an ESBT consisting of stock in one or more S corporations.

**Interest on tax deferred under the installment method for certain nondealer real property installment obligations.** If an obligation arising from the disposition of real property to which section 453A applies is outstanding at the close of the year, the estate or trust must include the interest due under section 453A(c) in the amount to be entered on line 7 of Schedule G, Form 1041, with the notation “Section 453A(c) interest.” Attach a schedule showing the computation.

**Form 4970, Tax on Accumulation Distribution of Trusts.** Include on this line any tax due on an accumulation distribution from a trust. To the left of the entry space, write “From Form 4970” and the amount of the tax.

**Form 8697, Interest Computation Under the Look-Back Method for Completed Long-Term Contracts.** Include the interest due under the look-back method of section 460(b)(2). To the left of the entry space, write “From Form 8697” and the amount of interest due.

**Form 8866, Interest Computation Under the Look-Back Method for Property Depreciated Under the Income Forecast Method.** Include the interest due under the look-back method of section 167(g)(2). To the left of the

entry space, write “From Form 8866” and the amount of interest due.

**Interest on deferral of gain from certain constructive ownership transactions.** Include the interest due under section 1260(b) on any deferral of gain from certain constructive ownership transactions. To the left of the entry space, write “1260(b)” and the amount of interest due.

**Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts.** If the estate or trust fails to receive the minimum distribution under section 4974, use Form 5329 to pay the excise tax. To the left of the entry space, write “From Form 5329” and the amount of the tax.

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## Other Information

### Question 1

If the estate or trust received tax-exempt income, figure the allocation of expenses between tax-exempt and taxable income on a separate sheet and attach it to the return. Enter only the deductible amounts on the return. Do not figure the allocation on the return itself. For more information, see the instructions for **Allocation of Deductions for Tax-Exempt Income** on page 15.

Report the amount of tax-exempt interest income received or accrued in the space provided below Question 1.

Also, include any exempt-interest dividends the estate or trust received as a shareholder in a mutual fund or other regulated investment company.

### Question 2

All salaries, wages, and other compensation for personal services must be included on the return of the person who earned the income, even if the income was irrevocably assigned to a trust by a contract assignment or similar arrangement.

The grantor or person creating the trust is considered the owner if he or she keeps “beneficial enjoyment” of or substantial control over the trust property. The trust’s income, deductions, and credits are allocable to the owner.

If you checked “Yes” for Question 2, see **Special Filing Instructions for Grantor Type Trusts, Pooled Income Funds, and Electing Small Business Trusts** on page 5.

### Question 3

Check the “Yes” box and enter the name of the foreign country if either 1 or 2 below applies.

1. At any time during the year the estate or trust had an interest in or signature or other authority over a bank, securities, or other financial account in a foreign country.

**Exception.** Check “No” if either of the following applies to the estate or trust:

- The combined value of the accounts was \$10,000 or less during the whole year or

- The accounts were with a U.S. military banking facility operated by a U.S. financial institution.

2. The estate or trust owns more than 50% of the stock in any corporation that owns one or more foreign bank accounts.

Get **Form TD F 90-22.1**, Report of Foreign Bank and Financial Accounts, to see if the estate or trust is considered to have an interest in or signature or other authority over a bank, securities, or other financial account in a foreign country.

If you checked "Yes" for Question 3, file Form TD F 90-22.1 by June 30, 2004, with the Department of the Treasury at the address shown on the form.

Form TD F 90-22.1 is not a tax return, so do not file it with Form 1041.

You may order Form TD F 90-22.1 by calling 1-800-829-3676 (1-800-TAX-FORM).

### Question 4

The estate or trust may be required to file **Form 3520**, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, if:

- It directly or indirectly transferred property or money to a foreign trust. For this purpose, any U.S. person who created a foreign trust is considered a transferor.
- It is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.
- It received a distribution from a foreign trust.

**Note:** An owner of a foreign trust must ensure that the trust files an annual information return on **Form 3520-A**, Annual Information Return of Foreign Trust With a U.S. Owner.

### Question 5

An estate or trust claiming an interest deduction for qualified residence interest (as defined in section 163(h)(3)) on seller-provided financing, must include on an attachment to the 2003 Form 1041 the name, address, and taxpayer identifying number of the person to whom the interest was paid or accrued (i.e., the seller).

If the estate or trust received or accrued such interest, it must provide identical information on the person liable for such interest (i.e., the buyer). This information does not need to be reported if it duplicates information already reported on Form 1098.

### Question 6

To make the section 663(b) election to treat any amount paid or credited to a beneficiary within 65 days following the close of the tax year as being paid or credited on the last day of that tax year, check the box. This election can be made by the fiduciary of a complex trust or the

executor of a decedent's estate. For the election to be valid, you must file Form 1041 by the due date (including extensions). Once made, the election is irrevocable.

### Question 7

To make the section 643(e)(3) election to recognize gain on property distributed in kind, check the box and see the instructions for Schedule D (Form 1041).

### Question 9

Generally, a beneficiary is a skip person if the beneficiary is in a generation that is two or more generations below the generation of the transferor to the trust.

To determine if a beneficiary that is a trust is a skip person, and for exceptions to the general rules, see the definition of a skip person in the instructions for Schedule R of Form 706.

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## Schedule I—Alternative Minimum Tax

### Changes To Note

- Part IV was revised to reflect the reduction in the maximum tax rate on net capital gain from 20% to 15% (the 10% rate was reduced to 5%) for sales and other dispositions and installment payments received after May 5, 2003.
- For tax years ending in 2003 or later, the alternative tax net operating loss deduction (ATNOLD) is generally limited to 90% of the estate's or trust's alternative minimum taxable income (figured without regard to the ATNOLD). See the Line 24 instructions for more information.

### General Instructions

Use Schedule I to compute:

1. The estate's or trust's alternative minimum taxable income;
2. The income distribution deduction on a minimum tax basis; and
3. The estate's or trust's alternative minimum tax (AMT).

### Who Must Complete

- Complete Schedule I, Parts I and II, if the estate or trust is required to complete Schedule B.
- Complete Schedule I if the estate's or trust's share of alternative minimum taxable income (Part I, line 29) exceeds \$22,500.
- Complete Schedule I if the estate or trust claims a credit on line 2b, 2c, or 2d of Schedule G.

### Recordkeeping

Schedule I contains adjustments and tax preference items that are treated differently for regular tax and AMT purposes. If you, as fiduciary for the estate or trust, completed a form to figure an item for regular tax purposes, you may have to complete it a second time for AMT purposes. Generally, the difference

between the amounts on the two forms is the AMT adjustment or tax preference item to enter on Schedule I. Except for Form 1116, any additional form completed for AMT purposes does not have to be filed with Form 1041.

For regular tax purposes, some deductions and credits may result in carrybacks or carryforwards to other tax years. Examples are: investment interest expense; a net operating loss deduction; a capital loss; and the foreign tax credit. Because these items may be refigured for the AMT, the carryback or carryforward amount may be different for regular and AMT purposes. Therefore, you should keep records of these different carryforward and carryback amounts for the AMT and regular tax. The AMT carryforward will be important in completing Schedule I for 2004.

### Credit for Prior Year Minimum Tax

Estates and trusts that paid alternative minimum tax in 2002, or had a minimum tax credit carryforward, may be eligible for a minimum tax credit in 2003. See Form 8801.

### Partners, Shareholders, etc.

An estate or trust that is a partner in a partnership or a shareholder in an S corporation must take into account its share of items of income and deductions that enter into the computation of its adjustments and tax preference items.

### Allocation of Deductions to Beneficiaries

The distributable net alternative minimum taxable income (DNAMTI) of the estate or trust does not include amounts of depreciation, depletion, and amortization that are allocated to the beneficiaries, just as the distributable net income (DNI) of the estate or trust does not include these items for regular tax purposes.

Report separately on line 12 of Schedule K-1 (Form 1041) any adjustments or tax preference items attributable to depreciation, depletion, and amortization that were allocated to the beneficiaries.

### Optional Write-Off for Certain Expenditures

There is no AMT adjustment for the following items if the estate or trust elects to deduct them ratably over the period of time shown for the regular tax:

- Circulation expenditures—3 years (section 173).
- Research and experimental expenditures—10 years (section 174).
- Intangible drilling costs—60 months (section 263(c)).
- Mining exploration and development costs—10 years (sections 616(a) and 617(a)).

The election must be made in the year the expenditure was made and may be revoked only with IRS consent. See section 59(e) for more details.



## Specific Instructions

### Part I—Estate's or Trust's Share of Alternative Minimum Taxable Income

#### Line 2—Interest

In determining the alternative minimum taxable income, qualified residence interest (other than qualified housing interest defined in section 56(e)) is not allowed.

If you completed Form 4952 for regular tax purposes, you may have an adjustment on this line. Refigure your investment interest expense on another Form 4952 as follows:

**Step 1.** On line 1 of Form 4952, add any interest expense allocable to specified private activity bonds issued after August 7, 1986, to the other interest expense. For a definition of "specified private activity bonds," see the instructions for line 8.

**Step 2.** On line 2, enter the AMT disallowed investment interest expense from 2002.

**Step 3.** When completing Part II of Form 4952, refigure gross income from property held for investment, any net gain from the disposition of property held for investment, and any investment expenses, taking into account all AMT adjustments and tax preference items that apply. Include any interest income and investment expenses from private activity bonds issued after August 7, 1986.

To figure the adjustment for line 2, subtract the total interest allowable for AMT purposes from the interest deduction claimed on line 10 of page 1. If the total interest expense allowed for AMT purposes is more than that allowed for regular tax purposes, enter the difference as a negative amount on line 2.

#### Line 3—Taxes

Enter any state, local, or foreign real property taxes; state or local personal property taxes; and state, local, or foreign income taxes that were included on line 11 of page 1.

#### Line 5—Refund of Taxes

Enter any refunds received in 2003 of taxes described for line 3 above that were deducted in a tax year after 1986.

#### Line 6—Depletion

Refigure the depletion deduction for AMT purposes by using only the income and deductions allowed for the AMT when refiguring the limit based on taxable income from the property under section 613(a) and the limit based on taxable income, with certain adjustments, under section 613A(d)(1). Also, the depletion deduction for mines, wells, and other natural deposits under section 611 is limited to the property's adjusted basis at the end of the year, as refigured for the AMT, unless the estate or trust is an independent producer or royalty owner claiming percentage depletion for oil and

gas wells. Figure this limit separately for each property. When refiguring the property's adjusted basis, take into account any AMT adjustments made this year or in previous years that affect basis (other than the current year's depletion).

Enter on line 6 the difference between the regular tax and AMT deduction. If the AMT deduction is more than the regular tax deduction, enter the difference as a negative amount.

#### Line 7—Net Operating Loss Deduction

Enter any net operating loss deduction (NOLD) from line 15a of page 1 as a positive amount.

#### Line 8—Interest From Specified Private Activity Bonds Exempt From the Regular Tax

Enter the interest earned from specified private activity bonds reduced (but not below zero) by any deduction that would have been allowable if the interest were includible in gross income for regular tax purposes. Specified private activity bonds are any qualified bonds (as defined in section 141) issued after August 7, 1986. See section 57(a)(5) for more information.

Exempt-interest dividends paid by a regulated investment company are treated as interest from specified private activity bonds to the extent the dividends are attributable to interest received by the company on the bonds, minus an allocable share of the expenses paid or incurred by the company in earning the interest.

#### Line 9—Qualified Small Business Stock

If the estate or trust claimed the exclusion under section 1202 for gain on qualified small business stock held more than 5 years, compute the amount to enter on line 9 as follows:

1. If the estate or trust sold qualified small business stock before May 6, 2003, multiply the excluded gain (as shown on Schedule D (Form 1041)) by 42% (.42).
2. If the estate or trust sold qualified small business stock after May 5, 2003, multiply the excluded gain (as shown on Schedule D (Form 1041)) by 7% (.07).
3. Combine the results and enter on line 9 as a positive amount.

#### Line 10—Exercise of Incentive Stock Options

For regular tax purposes, no income is recognized when an incentive stock option (as defined in section 422(b)) is exercised. However, this rule does not apply for AMT purposes. Instead, the estate or trust must generally include on line 10 the excess, if any, of:

1. The FMV of the stock acquired through exercise of the option (determined without regard to any lapse restriction) when its rights in the acquired stock first become transferable or when these rights are no longer subject to a substantial risk of forfeiture, over

2. The amount paid for the stock, including any amount paid for the option used to acquire the stock.

**Note:** *Even if the estate's or trust's rights in the stock are not transferable and are subject to a substantial risk of forfeiture, you may elect to include in AMT income the excess of the stock's FMV (determined without regard to any lapse restriction) over the exercise price upon the transfer to the estate or trust of the stock acquired through exercise of the option. See section 83(b) for more details. The election must be made no later than 30 days after the date of transfer.*

If the estate or trust acquired stock by exercising an option and it disposed of that stock in the same year, the tax treatment under the regular tax and the AMT is the same, and no adjustment is required.

Increase the AMT basis of any stock acquired through the exercise of an incentive stock option by the amount of the adjustment.

#### Line 11—Other Estates and Trusts

If the estate or trust is the beneficiary of another estate or trust, enter the adjustment for minimum tax purposes from line 9, Schedule K-1 (Form 1041).

#### Line 12—Electing Large Partnerships

If the estate or trust is a partner in an electing large partnership, enter on line 12 the amount from Schedule K-1 (Form 1065-B), box 6. Take into account any amount from Schedule K-1 (Form 1065-B), box 5, when figuring the amount to enter on line 15.

#### Line 13—Disposition of Property

Use this line to report any AMT adjustment related to the disposition of property resulting from refiguring:

1. Gain or loss from the sale, exchange, or involuntary conversion of property reported on **Form 4797**, Sales of Business Property;
2. Casualty gain or loss to business or income-producing property reported on **Form 4684**, Casualties and Thefts;
3. Ordinary income from the disposition of property not taken into account in **1** or **2** above or on any other line on Schedule I, such as a disqualifying disposition of stock acquired in a prior year by exercising an incentive stock option; and
4. Capital gain or loss (including any carryover that is different for the AMT) reported on Schedule D (Form 1041).



*The \$3,000 capital loss limitation for the regular tax applies separately for the AMT.*

First, figure any ordinary income adjustment related to **3** above. Then, refigure Form 4684, Form 4797, and Schedule D for the AMT, if applicable, by taking into account any adjustments you made this year or in previous years that

affect the estate's or trust's basis or otherwise result in a different amount for AMT. If the estate or trust has a capital loss after refiguring Schedule D for the AMT, apply the \$3,000 capital loss limitation separately to the AMT loss. For each of the 4 items listed above, figure the difference between the amount included in taxable income for the regular tax and the amount included in income for the AMT. Treat the difference as a negative amount if (a) both the AMT and regular tax amounts are zero or more and the AMT amount is less than the regular tax amount or (b) the AMT amount is a loss, and the regular tax amount is a smaller loss, or zero or more.

Enter on line 13 the combined adjustments for the 4 items above.

### Line 14—Depreciation of Assets Placed in Service After 1986

This section describes when depreciation must be refigured for the AMT and how to figure the amount to enter on line 14.

**Do not** include on this line any depreciation adjustment from:

- An activity for which the estate or trust is not at risk or income or loss from a partnership or an S corporation if the basis limitations under section 704(d) or 1366(d) apply. Take this adjustment into account on line 16.
- A tax shelter farm activity. Take this adjustment into account on line 23.
- A passive activity. Take this adjustment into account on line 15.

### What depreciation must be refigured for the AMT?

Generally, you must refigure depreciation for the AMT, including depreciation allocable to inventory costs, for:

- Property placed in service after 1998 that is depreciated for the regular tax using the 200% declining balance method (generally 3-, 5-, 7-, or 10-year property under the modified cost recovery system (MACRS)),
- Section 1250 property placed in service after 1998 that is **not** depreciated for the regular tax using the straight line method, and
- Tangible property placed in service after 1986 and before 1999. If the transitional election was made under section 203(a)(1)(B) of the Tax Reform Act of 1986, this rule applies to property placed in service after July 31, 1986.

### What depreciation is not refigured for the AMT?

- Do not refigure depreciation for the AMT for:
- Residential rental property placed in service after 1998.
  - Nonresidential real property with a class life of 27.5 years or more placed in service after 1998 that is depreciated for the regular tax using the straight line method.
  - Other section 1250 property placed in service after 1998 that is depreciated for the regular tax using the straight line method.
  - Property (other than section 1250 property) placed in service after 1998 that

is depreciated for the regular tax using the 150% declining balance method or the straight line method.

- Property for which you elected to use the alternative depreciation system (ADS) of section 168(g) for the regular tax.
- Property that is qualified property under section 168(k)(2) (property eligible for the special depreciation allowance). The special allowance is deductible for the AMT and there is also no adjustment required for any depreciation figured on the remaining basis of the qualified property. Property for which an election is in effect under section 168(k)(2)(C)(iii) to **not** have the special allowance apply is **not** qualified property. See the instructions for Form 4562 for the definition of qualified property.
- Motion picture films, videotapes, or sound recordings.
- Property depreciated under the unit-of-production method or any other method not expressed in a term of years.
- Qualified Indian reservation property.

### How is depreciation refigured for the AMT?

**Property placed in service before 1999.** Refigure depreciation for the AMT using ADS with the same convention used for the regular tax. See the table below for the method and recovery period to use.

| Property Placed in Service Before 1999  |   |
|---|---|
| IF the property is...   | THEN use the...   |
| Section 1250 property.  | Straight line method over 40 years.   |
| Tangible property (other than section 1250 property) depreciated using straight line for the regular tax. | Straight line method over the property's AMT class life.  |
| Any other tangible property.  | 150% declining balance method, switching to straight line the first tax year it gives a larger deduction, over the property's AMT class life. |

**Property placed in service after 1998.** Use the same convention and recovery period used for the regular tax. For property other than section 1250 property, use the 150% declining balance method, switching to straight line the first tax year it gives a larger deduction. For section 1250 property, use the straight line method.

### How is the AMT class life determined?

The class life used for the AMT is not necessarily the same as the recovery period used for the regular tax. The class lives for the AMT are listed in Rev. Proc. 87-56, 1987-2 C.B. 674, and in **Pub. 946**, How To Depreciate Property. Use 12 years for any tangible personal property not assigned a class life.

**TIP** See Pub. 946 for optional tables that can be used to figure AMT depreciation. Rev. Proc. 89-15, 1989-1 C.B. 816, has special rules for short tax years and for property disposed of before the end of the recovery period.

### How is the line 14 adjustment figured?

Subtract the AMT deduction for depreciation from the regular tax deduction and enter the result. If the AMT deduction is more than the regular tax deduction, enter the difference as a negative amount.

In addition to the AMT adjustment to your deduction for depreciation, you must also adjust the amount of depreciation that was capitalized, if any, to account for the difference between the rules for the regular tax and the AMT. Include on this line the current year adjustment to taxable income, if any, resulting from the difference.

### Line 15—Passive Activities

**CAUTION** Do not enter again elsewhere on this schedule any AMT adjustment or tax preference item included on this line.

For AMT purposes, the rules described in section 469 apply, except that in applying the limitations, minimum tax rules apply.

Refigure passive activity gains and losses on an AMT basis. Refigure a passive activity gain or loss by taking into account all AMT adjustments or tax preference items that pertain to that activity.

You may complete a second Form 8582 to determine the passive activity losses allowed for AMT purposes, but do not send this AMT Form 8582 to the IRS.

Enter the difference between the loss reported on page 1, and the AMT loss, if any.

**TIP** The amount of any passive activity loss that is not deductible (and is therefore carried forward) for AMT purposes is likely to differ from the amount (if any) that is carried forward for regular tax purposes. Therefore, it is essential that you retain adequate records for both AMT and regular tax purposes.

**Publicly traded partnerships (PTPs).** If the estate or trust had a loss from a PTP, refigure the loss using any AMT adjustments and tax preference items.

### Line 16—Loss Limitations

**CAUTION** If the loss is from a passive activity, use line 15 instead. If the loss is from a tax shelter farm activity (that is not passive), use line 23.

Refigure your allowable losses for AMT purposes from activities for which you are not at risk and basis limitations applicable to interests in partnerships and stock in S corporations, by taking into account your AMT adjustments and tax preference items. See sections 59(h), 465, 704(d), and 1366(d).

Enter the difference between the loss reported for regular tax purposes and the AMT loss. If the AMT loss is more than the loss reported for regular tax purposes, enter the adjustment as a negative amount.

### Line 17—Circulation Costs



*Do not make this adjustment for expenditures for which you elected the optional 3-year write-off period for regular tax purposes.*

Circulation expenditures deducted under section 173(a) for regular tax purposes must be amortized for AMT purposes over 3 years beginning with the year the expenditures were paid or incurred.

Enter the difference between the regular tax and AMT deduction. If the AMT deduction is greater, enter the difference as a negative amount.

If the estate or trust had a loss on property for which circulation expenditures have not been fully amortized for the AMT, the AMT deduction is the **smaller** of (a) the amount of the loss allowable for the expenditures had they remained capitalized or (b) the remaining expenditures to be amortized for the AMT.

### Line 18—Long-Term Contracts

For AMT purposes, the percentage of completion method of accounting described in section 460(b) generally must be used. However, this rule does not apply to any home construction contract (as defined in section 460(e)(6)).

**Note:** *Contracts described in section 460(e)(1) are subject to the simplified method of cost allocation of section 460(b)(4).*

Enter the difference between the AMT and regular tax income. If the AMT income is smaller, enter the difference as a negative amount.

### Line 19—Mining Costs



*Do not make this adjustment for costs for which you elected the optional 10-year write-off period under section 59(e) for regular tax purposes.*

Expenditures for the development or exploration of a mine or certain other mineral deposits (other than an oil, gas, or geothermal well) deducted under sections 616(a) and 617(a) for regular tax purposes must be amortized for AMT purposes over 10 years beginning with the year the expenditures were paid or incurred.

Enter the difference between the amount allowed for AMT purposes and the amount allowed for regular tax purposes. If the amount allowed for AMT purposes exceeds the amount deducted for regular tax purposes, enter the difference as a negative amount.

If the estate or trust had a loss on property for which mining expenditures have not been fully amortized for the AMT, the AMT deduction is the **smaller** of (a) the amount of the loss allowable for the expenditures had they remained capitalized or (b) the remaining expenditures to be amortized for the AMT.

### Line 20—Research and Experimental Costs



*Do not make this adjustment for costs paid or incurred in connection with an activity in which the estate or trust materially participated under the passive activity rules or for costs for which you elected the optional 10-year write-off for research and experimental expenditures under section 59(e) for regular tax purposes.*

Research and experimental expenditures deducted under section 174(a) for regular tax purposes generally must be amortized for AMT purposes over 10 years beginning with the year the expenditures were paid or incurred.

Enter the difference between the amount allowed for AMT purposes and the amount allowed for regular tax purposes. If the amount for AMT purposes exceeds the amount allowed for regular tax purposes, enter the difference as a negative amount.

If the estate or trust had a loss on property for which research and experimental costs have not been fully amortized for the AMT, the AMT deduction is the **smaller** of (a) the loss allowable for the costs had they remained capitalized or (b) the remaining costs to be amortized for the AMT.

### Line 21—Income From Certain Installment Sales Before January 1, 1987

The installment method does not apply for AMT purposes to any nondealer disposition of property that occurred after August 16, 1986, but before the first day of your tax year that began in 1987, if an installment obligation to which the proportionate disallowance rule applied arose from the disposition. Enter on line 21 the amount of installment sale income that was reported for regular tax purposes.

### Line 22—Intangible Drilling Costs Preference (IDCs)



*Do not make this adjustment for costs for which you elected the optional 60-month write-off under section 59(e) for regular tax purposes.*

IDCs from oil, gas, and geothermal wells are a preference to the extent that the excess IDCs exceed 65% of the net income from the wells. Figure the preference for all oil and gas properties separately from the preference for all geothermal properties.

Figure excess IDCs as follows:

1. Determine the amount of the estate's or trust's IDCs allowed for the regular tax under section 263(c), but do not include any section 263(c) deduction for nonproductive wells.

2. Subtract the amount that would have been allowed had you amortized these IDCs over a 120-month period starting with the month the well was placed in production.

**Note:** *Cost depletion can be substituted for the amount allowed using amortization over 120 months.*

Determine net income by reducing the gross income that the estate or trust received or accrued during the tax year from all oil, gas, and geothermal wells by the deductions allocable to those wells (reduced by the excess IDCs). When refiguring net income, use only income and deductions allowed for the AMT.

**Exception.** The preference for IDCs from oil and gas wells does not apply to taxpayers who are independent producers (i.e., not integrated oil companies as defined in section 291(b)(4)). However, this benefit may be limited. First, figure the IDC preference as if this exception did not apply. Then, for purposes of this exception, complete Schedule I through line 23, including the IDC preference and combine lines 1 through 23. If the amount of the IDC preference exceeds 40% of the total of lines 1 through 23, enter the excess on line 22 (the benefit of this exception is limited). Otherwise, do not enter an amount on line 22 (the estate's or trust's benefit from this exception is not limited).

### Line 23—Other Adjustments

Enter on line 23 the total of any other adjustments that apply including the following.

• **Depreciation figured using pre-1987 rules.**

For AMT purposes, use the straight line method to figure depreciation on real property. Use a recovery period of 19 years for 19-year real property and 15 years for low-income housing. Enter the excess of depreciation claimed for regular tax purposes over depreciation refigured using the straight line method. Figure this amount separately for each property and include on line 23 only positive amounts.

For leased personal property other than recovery property, enter the amount by which the regular tax depreciation using the pre-1987 rules exceeds the depreciation allowable using the straight line method. For leased 10-year recovery property and leased 15-year public utility property, enter the amount by which the depreciation deduction determined for regular tax purposes is more than the deduction allowable using the straight line method with a half-year convention, no salvage value, and a recovery period of 15 years (22 years for 15-year public utility property). Figure this amount separately for each property and include on line 23 only positive amounts.

• **Patron's adjustment.** Distributions the estate or trust received from a cooperative may be includible in income. Unless the distributions are nontaxable, include on line 23 the total AMT patronage dividend adjustment reported to the estate or trust from the cooperative.

• **Amortization of pollution control facilities.** The amortization deduction under section 169 must be refigured for the AMT. For facilities placed in service after 1986 and before 1999, figure the amortization deduction for the AMT using the ADS described in section 168(g). For facilities placed in service after 1998, figure the AMT deduction under MACRS using the straight line method. Enter the difference between the regular tax and AMT deduction. If the AMT amount is greater, enter the difference as a negative amount.

• **Tax shelter farm activities.** Figure this adjustment only if the tax shelter farm activity (as defined in section 58(a)(2)) is **not** a passive activity. If the activity is passive, include it with any other passive activities on line 15.

Refigure all gains and losses reported for the regular tax from tax shelter farm activities by taking into account any AMT adjustments and preferences. Determine tax shelter farm activity gain or loss for the AMT using the same rules used for the regular tax with the following modifications. No refigured loss is allowed, except to the extent an estate or trust is insolvent (see section 58(c)(1)). A refigured loss may not be used in the current tax year to offset gains from other tax shelter farm activities. Instead, any refigured loss must be suspended and carried forward indefinitely until (a) the estate or trust has a gain in a subsequent tax year from the same activity or (b) the activity is disposed of.

The AMT amount of any tax shelter farm activity loss that is not deductible and is carried forward is likely to differ from the regular tax amount. Keep adequate records for both the AMT and regular tax.

Enter the difference between the amount that would be reported for the activity on Schedule E or F for the AMT and the regular tax amount. If (a) the AMT loss is more than the regular tax loss, (b) the AMT gain is less than the regular tax gain, or (c) there is an AMT loss and a regular tax gain, then enter the adjustment as a negative amount.

Enter any adjustment for amounts reported on Schedule D, Form 4684, or Form 4797 for the activity on line 13 instead.

• **Alcohol fuel credit.** If the adjusted total income (line 17, of page 1) includes the amount of the alcohol fuel credit under section 87, include that amount as a negative amount on line 23.

• **Related adjustments.** AMT adjustments and tax preference items may affect deductions that are based on an income limit other than AGI or modified AGI (e.g., farm conservation

expenses). Refigure these deductions using the income limit as modified for the AMT. Include the difference between the regular tax and AMT deduction on line 23. If the AMT deduction is more than the regular tax deduction, include the difference as a negative amount.

**Note:** Do not make an adjustment on line 23 for an item you refigured on another line of Schedule I (e.g., line 6).

### Line 24—Alternative Tax Net Operating Loss Deduction (ATNOLD)

The ATNOLD is the sum of the alternative tax net operating loss (ATNOL) carryovers and carrybacks to the tax year, subject to the limitation explained below.

For tax years beginning after 1986, the net operating loss (NOL) under section 172(c) is modified for alternative tax purposes by (a) adding the adjustments made under sections 56 and 58 (subtracting if the adjustments are negative); and (b) reducing the NOL by any item of tax preference under section 57 (except the appreciated charitable contribution preference item). For an estate or trust that held a residual interest in a real estate mortgage investment conduit (REMIC), figure the ATNOLD without regard to any excess inclusion.

If this estate or trust is the beneficiary of another estate or trust that terminated in 2003, include any ATNOL carryover that was reported on line 13e of Schedule K-1 (Form 1041).

The estate's or trust's ATNOLD may be limited. To figure the ATNOLD limitation, first figure AMTI without regard to the ATNOLD. For this purpose, figure a tentative amount for line 6 of Schedule I by treating line 24 as if it were zero. Then, figure a tentative total by combining lines 1–23 of Schedule I using the line 6 tentative amount. The ATNOLD limitation is 90% of the tentative total.

Enter on line 24 the smaller of the ATNOLD or the ATNOLD limitation.

Any ATNOL not used because of the ATNOLD limitation can be carried back or forward. See section 172(b) for details.

The treatment of ATNOLs does not affect your regular tax NOL.

**Note:** If you elected under section 172(b)(3) to forego the carryback period for regular tax purposes, the election will also apply for the AMT.

### Line 29—Estate's or Trust's Share of Alternative Minimum Taxable Income

For an estate or trust that held a residual interest in a REMIC, line 29 may not be less than the estate's or trust's share of the amount on Schedule E (Form 1040), line 37, column (c). If that amount is larger than the amount you would otherwise enter on line 29, enter that amount instead and write "Sch. Q" on the dotted line next to line 29.

## Part II—Income Distribution Deduction on a Minimum Tax Basis

### Line 30—Adjusted Alternative Minimum Taxable Income

Generally, enter on line 30, Schedule I, the amount from line 25, Schedule I. However, if **both** line 4 on page 1 and line 25, Schedule I, are losses, enter on line 30, Schedule I, the smaller of those losses. If line 4 is zero or a gain and line 25 is a loss, enter zero on line 30, Schedule I.

### Line 31—Adjusted Tax-Exempt Interest

To figure the adjusted tax-exempt interest (including exempt-interest dividends received as a shareholder in a mutual fund or other regulated investment company), subtract the total of any:

1. Tax-exempt interest from line 2 of Schedule A of Form 1041 figured for AMT purposes and
2. Section 212 expenses allowable for AMT purposes allocable to tax-exempt interest, from the amount of tax-exempt interest received.

**Do not** subtract any deductions reported on lines 2 through 4.

Section 212 expenses that are directly allocable to tax-exempt interest are allocated only to tax-exempt interest. A reasonable proportion of section 212 expenses that are indirectly allocable to both tax-exempt interest and other income must be allocated to each class of income.

### Line 33

Reduce the amount on line 33 by any allocable section 1202 exclusion (as refigured for AMT purposes).

### Line 34

Enter any capital gains that were paid or permanently set aside for charitable purposes from the current year's income included on line 1 of Schedule A. Reduce the amount on line 34 by any allocable section 1202 exclusion (as refigured for AMT purposes).

### Lines 35 and 36

Capital gains and losses must take into account any basis adjustments from line 13, Part I.

### Line 41—Adjustment for Tax-Exempt Income

In figuring the income distribution deduction on a minimum tax basis, the estate or trust is not allowed a deduction for any item of DNAMTI (line 37) that is not included in the gross income of the estate or trust figured on an AMT basis. Thus, for purposes of figuring the allowable income distribution deduction on a minimum tax basis, the DNAMTI is figured without regard to any tax-exempt interest (except for amounts from line 8).

If tax-exempt interest is the only tax-exempt income included in the total

distributions (line 40), and the DNAMTI (line 37) is less than or equal to line 40, then enter on line 41 the amount from line 31.

If tax-exempt interest is the only tax-exempt income included in the total distributions (line 40), and the DNAMTI is more than line 40 (i.e., the estate or trust made a distribution that is less than the DNAMTI), then figure the adjustment by multiplying line 31 by a fraction, the numerator of which is the total distributions (line 40), and the denominator of which is the DNAMTI (line 37). Enter the result on line 41.

If line 40 includes tax-exempt income other than tax-exempt interest (except for amounts from line 8), figure line 41 by subtracting the total expenses allocable to tax-exempt income that are allowable for AMT purposes from tax-exempt income included on line 40.

Expenses that are directly allocable to tax-exempt income are allocated only to tax-exempt income. A reasonable proportion of expenses indirectly allocable to both tax-exempt income and other income must be allocated to each class of income.

#### Line 44—Income Distribution Deduction on a Minimum Tax Basis

Allocate the income distribution deduction figured on a minimum tax basis among the beneficiaries in the same manner as income was allocated for regular tax purposes. Report each beneficiary's share on line 7 of Schedule K-1 (Form 1041).

### Part III—Alternative Minimum Tax Computation

#### Line 53—Alternative Minimum Foreign Tax Credit

**TIP** To see if you need to figure the estate's or trust's AMT foreign tax credit, fill in line 55 of Schedule I as instructed. If the amount on line 55 is greater than or equal to the amount on line 52, the estate or trust does not owe the AMT. Enter zero on line 56 and see **Who Must Complete** on page 24 to find out if you must file Schedule I with Form 1041. However, even if the estate or trust does not owe AMT, you may need to complete line 53 to see if you have an AMT foreign tax credit carryback or carryforward to other tax years.

To figure the AMT foreign tax credit:

1. Complete and attach a separate AMT Form 1116, with the notation at the top, "Alt Min Tax" for each separate limitation category specified at the top of Form 1116.

**Note:** When applying the separate limitation categories, use the applicable AMT rate instead of the regular tax rate to determine if any income is "high-taxed."

2. If you (on behalf of the estate or trust) previously made or are making the

**simplified limitation election** (see below), skip Part I and enter on the AMT Form 1116, line 16, the same amount you entered on that line for the regular tax. If you did not complete Form 1116 for the regular tax and you previously made or are making the simplified limitation election (on behalf of the estate or trust), complete Part I and lines 14 through 16 of the AMT Form 1116 using regular tax amounts.

If the election does not apply, complete Part I, using only income and deductions allowed for the AMT that are attributable to sources outside the United States. If the Instructions for Form 1116 require you to adjust your foreign source capital gains or losses, complete Worksheet A or B or follow the instructions for **Capital Gains and Losses** in **Pub. 514**, Foreign Tax Credit for Individuals, (whichever is applicable) and the Worksheet for Line 17 for the AMT. If you are required to complete an AMT Worksheet for line 17, follow the instructions under **5** below.

3. Complete Part II and lines 9 through 13 of the AMT Form 1116. Use the estate's or trust's AMT foreign tax credit carryover, if any, on line 10.

4. If the simplified limitation election does not apply, complete lines 14 through 16 of the AMT Form 1116.

5. If you did not complete Schedule D (Form 1041) for the regular tax and did not complete Part IV of Schedule I of Form 1041, enter the AMTI from Schedule I, line 29, on line 17 of the AMT Form 1116 and go to **6** below. Otherwise, follow these steps to complete, for the AMT, the Worksheet for line 17 in the Form 1116 instructions:

- a. Enter the amount from Schedule I of Form 1041, line 29, on line 1 of the AMT Worksheet for line 17.

- b. Complete a Schedule D for the AMT as explained in the instructions for lines 58, 59, 60, 64 and 67 on this page (or, if you already completed an AMT Schedule D to complete Part IV of Schedule I, use that Schedule D). Next, enter the amount from Schedule I, line 51, on line 18 of your AMT Schedule D or line 1 of the AMT Schedule D Tax Worksheet. Then, complete lines 24 through 45 of the AMT Schedule D (you may skip lines 30, 34, 36, and 44) or lines 14 through 46 of the AMT Schedule D Tax Worksheet (you may skip lines 22, 26, 28, 36, 38, and 44).

- c. Complete the rest of the AMT Worksheet for Line 17 using amounts from the AMT Schedule D.

6. Enter the amount from Schedule I, line 52, on the AMT Form 1116, line 19. Complete lines 18, 20, and 21 of the AMT Form 1116.

7. Complete Part IV of the **first** AMT Form 1116.

Follow the instructions below to figure the amount to enter on line 53 of Schedule I of Form 1041.

If you have no entry on line 24 of Schedule I of Form 1041, and no

intangible drilling costs (IDCs) (or the exception for IDCs does not apply to the estate or trust—see the instructions for line 22 on page 27), enter on line 53 of Schedule I the **smaller** of:

- 90% of line 52 of Schedule I or
- The amount from line 33 of the first AMT Form 1116.

If you have an entry on line 24 or the exception for IDCs applies to the estate or trust:

1. Figure the amount of tax that would be on line 52 if line 24 were zero and the exception did not apply.

2. Multiply the amount from **1** above by 10%.

3. Subtract the amount from **2** above from the tax on line 52.

4. Enter on Schedule I, line 53, the **smaller** of the amount from **3** above or the amount from line 33 of the first AMT Form 1116.

**AMT foreign tax credit carryback and carryforward.** If the AMT foreign tax credit is limited, any unused amount can be carried back or forward in accordance with sections 59(a)(2)(B) and 904(c).

**Note:** The election to forego the carryback period for regular tax purposes also applies for the AMT.

**Simplified limitation election.** The estate or trust may elect to use a simplified section 904 limitation to figure its AMT foreign tax credit. To do so, use the estate's or trust's regular tax income for Form 1116, Part I, instead of refiguring the estate's or trust's foreign source income for the AMT, as described in **2** on this page. The estate or trust must make the election for the first tax year after 1997 for which it claims an alternative minimum tax foreign tax credit. If it does not make the election for that year, it may not make it for a later year. Once made, the election applies to all later tax years and may be revoked only with IRS consent.

#### Part IV—Line 52 Computation Using Maximum Capital Gains Rates

##### Lines 58, 59, 60, 64, and 67

If you figured the estate's or trust's tax using the **Qualified Dividends Tax Worksheet** (instead of Schedule D, Part V, or the Schedule D Tax Worksheet) then:

- Enter on lines 58 and 60 the amount from line 4 of the Qualified Dividends Tax Worksheet;
- Skip line 59;
- Enter on line 64 the amount, if any, from line 8 of the worksheet; and
- Enter on line 67 the amount, if any, from line 2 of the worksheet.

If you used Schedule D or the Schedule D Tax Worksheet, you generally may enter the amounts as instructed on Schedule I, lines 58, 59, 60, and 67. But **do not** use those amounts if either of the following applies:

1. Any gain or loss on Schedule D is different for the AMT (for example, because the AMT basis was different due to depreciation adjustments or an incentive stock option adjustment or the AMT capital loss carryover from 2002 was different).

2. You did not complete Part V of Schedule D because Form 1041, line 22, was zero or less.

If 1 or 2 above applies, complete a Schedule D for the AMT. If 1 above applies, refigure the amounts for Schedule D, Parts I, II, III, and IV for the AMT; otherwise, use the regular tax amounts.

Next, complete lines 19 through 23 and 28 of the AMT Schedule D (lines 2 through 13 and 20 of the AMT Schedule D Tax Worksheet, if applicable). Use amounts from the AMT Schedule D or AMT Schedule D Tax Worksheet to complete Schedule I, lines 58, 59, 60, and 67. Keep the AMT Schedule D and worksheet for your records but **do not** attach the AMT Schedule D to Form 1041.

If you did not complete line 27 of Schedule D (or line 19 of the Schedule D Tax Worksheet) for the regular tax, enter zero on Schedule I, line 64.

**Note:** *Do not decrease the estate's or trust's section 1202 exclusion by the amount, if any, included on line 9.*

### Line 71

Generally, you may enter the amount from Schedule D, line 15c, column (2), on Schedule I, line 71. However, if the qualified 5-year gain is different for the AMT (for example, because of a different basis), you must complete an **AMT Qualified 5-Year Gain Worksheet** (on page 33). If the amount on any line of the worksheet is different for the AMT, use the AMT amount instead of the regular tax amount. Enter the estate's or trust's portion on Schedule I, line 71.

## Schedule D (Form 1041)— Capital Gains and Losses

### Changes To Note

- The 20% maximum tax rate on net capital gain (the excess of net long-term capital gain over net short-term capital loss) has been reduced to 15%, and the 10% rate has been reduced to 5%, for sales and other dispositions after May 5, 2003 (and installment payments received after that date). The 25% rate on unrecaptured section 1250 gain and the 28% rate on collectibles gain and section 1202 gain have not changed.
- The 8% maximum capital gains tax rate for qualified 5-year gain has been repealed for sales and other dispositions after May 5, 2003 (and installment payments received after that date). Instead, gain from these transactions will be taxed at the 5% maximum capital gains tax rate.

- Any 28% rate gain is now figured on a worksheet and entered in the appropriate column of Schedule D, line 15e.

## General Instructions

### Purpose of Form

Use Schedule D (Form 1041) to report gains and losses from the sale or exchange of capital assets by an estate or trust.

To report the sale or exchange of property used in a trade or business, involuntary conversions (other than casualties and thefts), and certain ordinary gains and losses, see Form 4797 and related instructions.

If property is involuntarily converted because of a casualty or theft, use Form 4684.

Section 1256 contracts and straddles are reported on **Form 6781**, Gains and Losses From Section 1256 Contracts and Straddles.

### Capital Asset

Each item of property held by the estate or trust (whether or not connected with its trade or business) is a capital asset except:

- Inventoriable assets or property held primarily for sale to customers;
- Depreciable or real property used in a trade or business, even if it is fully depreciated;
- Certain copyrights, literary, musical, or artistic compositions, letters or memoranda, or similar property;
- Accounts or notes receivable acquired in the ordinary course of a trade or business for services rendered or from the sale of inventoriable assets or property held primarily for sale to customers;
- Certain U.S. Government publications not purchased at the public sale price;
- Certain "commodities derivative financial instruments" held by a dealer (see section 1221(a)(6));
- Certain hedging transactions entered into in the normal course of a trade or business (see section 1221(a)(7)); and
- Supplies regularly used in a trade or business.

You may find additional helpful information in the following publications:

- **Pub. 544**, Sales and Other Dispositions of Assets, and
- **Pub. 551**, Basis of Assets.

### Short-Term or Long-Term

Separate the capital gains and losses according to how long the estate or trust held or owned the property. The holding period for short-term capital gains and losses is 1 year or less. The holding period for long-term capital gains and losses is more than 1 year. Property acquired by a decedent's estate from the decedent is considered as held for more than 1 year.

When you figure the length of the period the estate or trust held property, begin counting on the day after the estate or trust acquired the property and include

the day the estate or trust disposed of it. Use the trade dates for the date of acquisition and sale of stocks and bonds traded on an exchange or over-the-counter market.

### Section 643(e)(3) Election

For noncash property distributions, a fiduciary may elect to have the estate or trust recognize gain or loss in the same manner as if the distributed property had been sold to the beneficiary at its FMV. The distribution deduction is the property's FMV. This election applies to all distributions made by the estate or trust during the tax year and, once made, may be revoked only with IRS consent.

Note that section 267 does not allow a trust or a decedent's estate to claim a deduction for any loss on property to which a section 643(e)(3) election applies. In addition, when a trust or a decedent's estate distributes depreciable property, section 1239 applies to deny capital gains treatment for any gain on property to which a section 643(e)(3) election applies.

### Related Persons

A trust cannot deduct a loss from the sale or exchange of property directly or indirectly between any of the following:

- A grantor and a fiduciary of a trust;
- A fiduciary and a fiduciary or beneficiary of another trust created by the same grantor;
- A fiduciary and a beneficiary of the same trust;
- A trust fiduciary and a corporation of which more than 50% in value of the outstanding stock is owned directly or indirectly by or for the trust or by or for the grantor of the trust; or
- An executor of an estate and a beneficiary of that estate, except when the sale or exchange is to satisfy a pecuniary bequest (i.e., a bequest of a sum of money).

### Items for Special Treatment

The following items may require special treatment:

- Wash sales of stock or securities (including contracts or options to acquire or sell stock or securities) (section 1091).
- Gain or loss on options to buy or sell (section 1234).
- Certain real estate subdivided for sale that may be considered a capital asset (section 1237).
- Gain on disposition of stock in an interest charge domestic international sales corporation (section 995(c)).
- Gain on the sale or exchange of stock in certain foreign corporations (section 1248).
- Sales of stock received under a qualified public utility dividend reinvestment plan. See Pub. 550 for details.
- Transfer of appreciated property to a political organization (section 84).
- Disposition of market discount bonds (section 1276).

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

- The sale of qualified empowerment zone assets acquired after December 21, 2000, that the estate or trust held for more than 1 year, if you elect to postpone gain by purchasing other qualified empowerment zone assets during the 60-day period that began on the date of the sale. See Pub. 550 and Pub. 954.

- If qualified dividends include extraordinary dividends, any loss on the sale or exchange of the stock is a long-term capital loss to the extent of the extraordinary dividends. An extraordinary dividend is a dividend that is at least 10% (5% in the case of preferred stock) of the basis in the stock.

### Constructive Sales Treatment for Certain Appreciated Positions

Generally, the estate or trust must recognize gain (but not loss) on the date it enters into a constructive sale of any appreciated position in stock, a partnership interest, or certain debt instruments as if the position were disposed of at FMV on that date.

The estate or trust is treated as making a constructive sale of an appreciated position when it (or a related person, in some cases) does one of the following:

- Enters into a short sale of the same or substantially identical property (i.e., a "short sale against the box").
- Enters into an offsetting notional principal contract relating to the same or substantially identical property.
- Enters into a futures or forward contract to deliver the same or substantially identical property.
- Acquires the same or substantially identical property (if the appreciated position is a short sale, offsetting notional principal contract, or a futures or forward contract).

**Exception.** Generally, constructive sale treatment **does not** apply if:

- The estate or trust closed the transaction before the end of the 30th day after the end of the year in which it was entered into,
- The estate or trust held the appreciated position to which the transaction relates throughout the 60-day period starting on the date the transaction was closed, **and**
- At no time during that 60-day period was the estate's or trust's risk of loss reduced by holding certain other positions.

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

### Exclusion of Gain on Qualified Small Business Stock (Section 1202)

Section 1202 provides for an exclusion of 50% of the gain on the sale or exchange

of qualified small business (QSB) stock. The section 1202 exclusion applies **only** to qualified small business stock held for more than 5 years. To be **qualified small business stock**, the stock must meet **all** of the following tests:

- It must be stock in a C corporation (i.e., 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 estate or trust 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 estate or trust may meet the test if it acquired the stock from another person who met this test (such as by gift or at death) or through a conversion or exchange of qualified small business stock the estate or trust held.
- During substantially all the time the estate or trust 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, 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 section 1202.

**Pass-through entities.** If the estate or trust held an interest in a pass-through entity (a partnership, S corporation, mutual fund, or other regulated investment company) that sold qualified small business stock, the estate or trust generally must have held the interest on the date the pass-through entity acquired the qualified small business stock and at all times thereafter until the stock was sold to qualify for the exclusion.

**How to report.** Report in column (f) of line 6 the entire gain realized on the sale of qualified small business stock. Complete all other columns as indicated. Directly below the line on which you reported the gain, enter in column (a) "Section 1202 exclusion," and enter as a (loss) in column (f) the amount of the allowable exclusion. On line 2 of the 28% Rate Gain Worksheet, include an amount equal to the section 1202 exclusion. Also, see the instructions for Schedule I, line 9, for information on the amount of the exclusion to include on Schedule I.

**Gain from Form 1099-DIV.** If the estate or trust received a Form 1099-DIV with a gain in box 2e, part or all of that gain (which is also included in box 2a) may be eligible for the section 1202 exclusion. In column (a) of line 6, enter the name of the corporation whose stock was sold. In column (f), enter the amount of the allowable exclusion as a (loss). Also, include the amount of the allowable exclusion as a gain on line 4 of the 28% Rate Gain Worksheet.

**Gain from Form 2439.** If the estate or trust received a **Form 2439**, Notice to Shareholder of Undistributed Long-Term Capital Gains, with a gain in box 1e, part or all of that gain (which is also included in box 1a) may be eligible for the section 1202 exclusion. In column (a) of line 6, enter the name of the corporation whose stock was sold. In column (f), enter the amount of the allowable exclusion as a (loss). Also, include the amount of the allowable exclusion as a gain on line 4 of the 28% Rate Gain Worksheet.

**Gain from an installment sale of QSB stock.** If all payments are not received in the year of sale, a sale of QSB stock that is not traded on an established securities market generally is treated as an installment sale and is reported on Form 6252. Part or all of any gain from the sale that is reported on Form 6252 for the current year may be eligible for the section 1202 exclusion. In column (a) of line 6, enter the name of the corporation whose stock was sold. In column (f), enter the amount of your allowable exclusion as a loss. Also, include the amount of your allowable exclusion as a gain on line 3 of the 28% Rate Gain Worksheet.

**Rollover of gain from qualified small business stock.** If the estate or trust held qualified small business stock (as

defined above) for more than 6 months, it may elect to postpone gain if it purchased other qualified small business stock during the 60-day period that began on the date of the sale.

The estate or trust 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.

The estate or trust must make the election no later than the due date (including extensions) for filing Form 1041 for the tax year in which the stock was sold. If the original Form 1041 was filed on time, the election may be made on an amended return filed no later than 6 months after the due date of the original return (excluding extensions). Write "Filed pursuant to section 301.9100-2" at the top of the amended return, and file it at the same address used for the original Form 1041.

To make the election, report the entire gain realized on the sale on line 1 or 6. Directly below the line on which you reported the gain, enter in column (a) "Section 1045 Rollover" and enter as a (loss) in column (f) the amount of the postponed gain.

## Specific Instructions

### Lines 1 and 6

**Short-term and long-term capital gains and losses.** Enter all sales of stocks, bonds, etc.

**Redemption of stock to pay death taxes.** If stock is redeemed under the provisions of section 303, list and identify it on line 6 and give the name of the decedent and the IRS office where the estate tax or generation-skipping transfer tax return was filed.

If you are reporting capital gain from a lump-sum distribution, see the instructions for Form 4972 for information about the Federal estate tax.

### Column (d)—Sales Price

Enter 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 estate or trust on Form 1099-B or similar statement. However, if the estate or trust was advised that gross proceeds less commissions and option premiums were reported to the IRS, enter that net amount in column (d).

### Column (e)—Cost or Other Basis

**Basis of trust property.** Generally, the basis of property acquired by gift is the same as the basis in the hands of the donor. If the FMV of the property at the time it was transferred to the trust is less than the transferor's basis, then the FMV is used for determining any loss on disposition.

If the property was transferred to the trust after 1976, and a gift tax was paid under Chapter 12, then increase the donor's basis as follows:

Multiply the amount of the gift tax paid by a fraction, the numerator of which is the net appreciation in value of the gift (defined below), and the denominator of which is the amount of the gift. For this purpose, the **net appreciation in value of the gift** is the amount by which the FMV of the gift exceeds the donor's adjusted basis.

**Basis of decedent's estate property.** Generally, the basis of property acquired by a decedent's estate is the FMV of the property at the date of the decedent's death, or the alternate valuation date if the executor elected to use an alternate valuation under section 2032.

See Pub. 551 for a discussion of the valuation of qualified real property under section 2032A.

**Basis of assets held on January 1, 2001, where an election to recognize gain was made.** If you elected on behalf of an estate or trust to recognize gain on an asset held on January 1, 2001, the basis in the asset is its closing market price or fair market value, whichever applies, on the date of the deemed sale and reacquisition, whether the deemed sale resulted in a gain or an unallowed loss.

**Adjustments to basis.** Before figuring any gain or loss on the sale, exchange, or other disposition of property owned by the estate or trust, adjustments to the property's basis may be required.

Some items that may increase the basis include:

1. Broker's fees and commissions.
2. Reinvested dividends that were previously reported as income.
3. Reinvested capital gains that were previously reported as income.
4. Costs that were capitalized.
5. Original issue discount that has been previously included in income.

Some items that may decrease the basis include:

1. Nontaxable distributions that consist of return of capital.
2. Deductions previously allowed or allowable for depreciation.
3. Casualty or theft loss deductions.

See Pub. 551 for additional information.

See section 852(f) for treatment of load charges incurred in acquiring stock in a regulated investment company.

**Carryover basis.** Carryover basis determined under repealed section 1023 applies to property acquired from a decedent who died after December 31, 1976, and before November 7, 1978, only if the executor elected it on a **Form 5970-A, Election of Carryover Basis**, that was filed on time.

### Column (f)—Gain or (Loss)

Make a separate entry in this column for each transaction reported on lines 1 and 6 and any other lines that apply to the estate or trust. For lines 1 and 6, subtract the amount in column (e) from the amount

in column (d). Enter negative amounts in parentheses.

### Column (g)—Post-May 5 Gain or (Loss)

Enter all gains and losses reported in column (f) from sales, exchanges, or conversions (including installment payments received) after May 5, 2003. However, do not include gain attributable to unrecaptured section 1250 gain, collectibles gains and losses, or eligible gain on qualified small business stock.

### Lines 2 and 7

**Undistributed capital gains.** Include on line 7, column (f), the amount from box 1a of Form 2439. This represents the estate's or trust's share of the undistributed long-term capital gains of the regulated investment company (mutual fund) or real estate investment trust.

Include on line 7, column (g), the amount, if any, from box 1b of Form 2439. If there is an amount in box 1c of Form 2439, include that amount on line 5 of the **Qualified 5-Year Gain Worksheet** on page 33 if you are required to complete line 15c, column (2) of Schedule D. If there is an amount in box 1d of Form 2439, include that amount on line 11 of the **Unrecaptured Section 1250 Gain Worksheet** on page 34 if you are required to complete line 15d, column (2) of Schedule D. If there is an amount in box 1e of Form 2439, see **Exclusion of Gain on Qualified Small Business Stock (Section 1202)** on page 31.

Enter on Form 1041, line 24f, the tax paid as shown in box 2 of Form 2439. Add to the basis of your stock the excess of the amount included in income over the amount of the credit for tax paid. See Pub. 550 for more details.



*The instructions above assume the estate or trust is a cash basis calendar year taxpayer.*

**Installment sales.** If the estate or trust sold property (other than publicly traded stocks or securities) at a gain during the tax year and will receive a payment in a later tax year, you generally report the sale on the installment method and file **Form 6252, Installment Sale Income**, unless you elect not to do so.

Also, use Form 6252 to report any payment received in 2003 from a sale made in an earlier tax year that was reported on the installment method.

To elect out of the installment method, report the full amount of the gain on a timely filed return (including extensions). If the original return was filed on time, the election may be made on an amended return filed no later than 6 months after the due date of the original return (excluding extensions). Write "Filed pursuant to section 301.9100-2" at the top of the amended return, and file it at the same address used for the original Form 1041.



**Exchange of "like-kind" property.**

Generally, no gain or loss is recognized when property held for productive use in a trade or business or for investment is exchanged solely for property of a like-kind to be held either for productive use in a trade or business or for investment. However, if a trust exchanges like-kind property with a related person (see **Related Persons** on page 30), and before 2 years after the date of the last transfer that was part of the exchange the related person disposes of the property, or the trust disposes of the property received in exchange from the related person, then the original exchange will not qualify for nonrecognition. See section 1031(f) for exceptions.

Complete and attach **Form 8824**, Like-Kind Exchanges, to Form 1041 for each exchange.

**Line 9—Capital Gain Distributions**

Enter as a long-term capital gain on line 9, column (f), the **total** capital gain distributions paid during the year, regardless of how long the estate or trust held its investment. This amount is shown in box 2a of Form 1099-DIV. If there is an amount in box 2b of Form 1099-DIV, include that amount on line 9, column (g). If there is an amount in box 2c, include that amount on line 5 of the **Qualified 5-Year Gain Worksheet** (below) if you are required to complete the worksheet. If there is an amount in box 2d, include that amount on line 11 of the **Unrecaptured Section 1250 Gain Worksheet** on page 34 if you are required to complete the worksheet. If there is an amount in box 2e, see **Exclusion of Gain on Qualified**

**Small Business (QSB) Stock** on page 31.



*The instructions above assume the estate or trust is a cash basis calendar year taxpayer.*

**Line 14a, Column (1)—Beneficiaries' Net Short-Term Capital Gain or Loss**

Enter the amount of net short-term capital gain or loss allocable to the beneficiary or beneficiaries. Include only those short-term capital losses that are taken into account in determining the amount of gain from the sale or exchange of capital assets that is paid, credited, or required to be distributed to any beneficiary during the tax year. See Regulations section 1.643(a)-3 for more information about allocation of capital gains and losses.

If the losses from the sale or exchange of capital assets are more than the gains, all of the losses must be allocated to the estate or trust and none are allocated to the beneficiaries.

**Line 14a, Column (2)—Estate's or Trust's Net Short-Term Capital Gain or Loss**

Enter the amount of the net short-term capital gain or loss allocable to the estate or trust. Include any capital gain paid or permanently set aside for a charitable purpose specified in section 642(c).

**Line 14a, Column (3)—Total**

Enter the total of the amounts entered in columns (1) and (2). The amount in column (3) should be the same as the amount on line 5.

**Line 14b(1)—Beneficiaries' Net Short-Term Gain (Post-May 5, 2003)**

If line 5a is a gain, enter the beneficiaries' allocable share of post-May 5, 2003, net short-term gain, if any. Reduce that amount by the beneficiaries' allocable share of the loss on line 12, if any, and enter the result. If zero or less, leave line 14b(1) blank.

**Line 14b(2)—Estate's or Trust's Net Short-Term Loss (Post-May 5, 2003)**

If line 5a is a loss, enter the estate's or trust's allocable share of post-May 5, 2003, net short-term loss. Otherwise, enter -0-.

**Line 15a—Net Long-Term Capital Gain or Loss**

Allocate the net long-term capital gain or loss on line 15a in the same manner as the net short-term capital gain or loss on line 14a. However, **do not** take the section 1202 exclusion on gain from the sale or exchange of qualified small business stock into account when figuring net long-term capital gain or loss allocable to the beneficiaries.

**Line 15b—Net Long-Term Gain (Post-May 5, 2003)**

**Beneficiaries.** If line 12 is a gain, enter the beneficiaries' allocable share, if any, of the gain. Reduce that amount by the beneficiaries' allocable share of the loss on line 5a, if any, and enter the result. If zero or less, leave the line blank.

**Estate or trust.** Enter the estate's or trust's allocable share of gain from line 12, if any.

**Qualified 5-Year Gain Worksheet—Line 15c**

*Keep for Your Records*

|   |          |
|---|----------|
| 1. Enter the total of all gains reported on line 6, column (f), of Schedule D from property held more than 5 years and disposed of before May 6, 2003. <b>Do not</b> reduce these gains by any losses . . . . .   | 1. _____ |
| 2. Enter the total of all gains from property held more than 5 years and disposed of before May 6, 2003, from Form 4797, Part I, but <b>only</b> if Form 4797, line 7, column (g), is more than zero. <b>Do not</b> reduce these gains by any losses . . . . .  | 2. _____ |
| 3. Enter the total of all capital gains from property held more than 5 years and disposed of before May 6, 2003, from Form 4684, line 4, but <b>only</b> if Form 4684, line 15, is more than zero. <b>Do not</b> reduce these gains by any losses . . . . .   | 3. _____ |
| 4. Enter the total of all capital gains from property held more than 5 years and disposed of before May 6, 2003, from Form 6252; Form 6781, Part II; and Form 8824. <b>Do not</b> reduce these gains by any losses . . . . .  | 4. _____ |
| 5. Enter the total of any qualified 5-year gain reported to the estate or trust on: <ul style="list-style-type: none"> <li>• Form 1099-DIV, box 2c;</li> <li>• Form 2439, box 1c; and</li> <li>• Schedule K-1 from a partnership, S corporation, estate, or trust (<b>do not</b> include gains from section 1231 property; take them into account on line 2 above, but <b>only</b> if Form 4797, line 7, column (g), is more than zero).</li> </ul> | 5. _____ |
| 6. Add lines 1 through 5 . . . . .  | 6. _____ |
| 7. Enter the part, if any, of the gain on line 6 that is: <ul style="list-style-type: none"> <li>• Attributable to 28% rate gain <b>or</b></li> <li>• Included on line 6, 10, 11, or 12 of the <b>Unrecaptured Section 1250 Gain Worksheet</b> on page 34.</li> </ul>   | 7. _____ |
| 8. <b>Qualified 5-year gain.</b> Subtract line 7 from line 6. Enter the result here and in the appropriate columns of Schedule D, line 15c. . . . .   | 8. _____ |

**Line 15c—Qualified 5-Year Gain**

Qualified 5-year gain is long-term capital gain (other than 28% rate gain or gain on lines 6, 10, 11, and 12 of the **Unrecaptured Section 1250 Gain Worksheet**) from the sale or other disposition of property before May 6, 2003, that was held more than 5 years. Qualified 5-year gain is taxed at 8% to the extent the gain would otherwise be taxed at 10%. To figure qualified 5-year gain, complete the worksheet on page 33 if any of the following apply:

- The estate or trust sold or otherwise disposed of property before May 6, 2003, at a gain, and that it had held for more than 5 years.
- The estate or trust received a Schedule K-1 from an estate, trust, partnership, or S corporation that reports "qualified 5-year gain."
- The estate or trust received a Form 1099-DIV (or Form 2439) with "qualified 5-year gain" reported in box 2c (box 1c of Form 2439).
- The estate or trust received payments before May 6, 2003, from an installment sale of property that it had held for more

than 5 years when it entered into the installment sale.

**Line 15d—Unrecaptured Section 1250 Gain**

Complete the worksheet on this page if any of the following apply.

- During the tax year, the estate or trust sold or otherwise disposed of section 1250 property (generally, real property that was depreciated) held more than 1 year.
- The estate or trust received installment payments during the tax year for section 1250 property held more than 1 year for which it is reporting gain on the installment method.
- The estate or trust received a Schedule K-1 from an estate or trust, partnership, or S corporation that shows "unrecaptured section 1250 gain" reportable for the tax year.
- The estate or trust received a Form 1099-DIV or Form 2439 from a real estate investment trust or regulated investment company (including a mutual fund) that reports "unrecaptured section 1250 gain" for the tax year.

- The estate or trust reported a long-term capital gain from the sale or exchange of an interest in a partnership that owned section 1250 property.

**Instructions for the Unrecaptured Section 1250 Gain Worksheet**

**Lines 1 through 3.** If the estate or trust had more than one property described on line 1, complete lines 1 through 3 for each property on a separate worksheet. Enter the total of the line 3 amounts for all properties on line 3 and go to line 4.

**Line 4.** To figure the amount to enter on line 4, follow the steps below for each installment sale of trade or business property held more than 1 year.

**Step 1.** Figure the **smaller** of (a) the depreciation allowed or allowable or (b) the total gain for the sale. This is the **smaller** of line 22 or line 24 of the 2003 Form 4797 (or the comparable lines of Form 4797 for the year of sale) for that property.

**Step 2.** Reduce the amount figured in **step 1** by any section 1250 ordinary income recapture for the sale. This is the amount from line 26g of the 2003 Form

**Unrecaptured Section 1250 Gain Worksheet—Line 15d**

*Keep for Your Records*

**If the estate or trust is not reporting a gain on Form 4797, line 7, column (g), skip lines 1 through 9 and go to line 10.**

|   |     |         |
|---|-----|---------|
| 1. If the estate or trust has a section 1250 property in Part III of Form 4797 for which you made an entry in Part I of Form 4797 (but not on Form 6252), enter the <b>smaller</b> of line 22 or line 24 of Form 4797 for that property. If the estate or trust did not have any such property, go to line 4. If it had more than one such property, see instructions . . . . . | 1.  | _____   |
| 2. Enter the amount from Form 4797, line 26g, for the property for which you made an entry on line 1 . . . .  | 2.  | _____   |
| 3. Subtract line 2 from line 1 . . . . .  | 3.  | _____   |
| 4. Enter the total unrecaptured section 1250 gain included on line 26 or line 37 of Form(s) 6252 from installment sales of trade or business property held more than 1 year (see instructions) . . . . .  | 4.  | _____   |
| 5. Enter the total of any amounts reported to the estate or trust on a Schedule K-1 from a partnership or an S corporation as "unrecaptured section 1250 gain" . . . . .  | 5.  | _____   |
| 6. Add lines 3 through 5 . . . . .  | 6.  | _____   |
| 7. Enter the <b>smaller</b> of line 6 or the gain from Form 4797, line 7, column (g) . . . . .  | 7.  | _____   |
| 8. Enter the amount, if any, from Form 4797, line 8, column (g) . . . . .   | 8.  | _____   |
| 9. Subtract line 8 from line 7. If zero or less, enter -0- . . . . .  | 9.  | _____   |
| 10. Enter the amount of any gain from the sale or exchange of an interest in a partnership attributable to unrecaptured section 1250 gain (see instructions) . . . . .  | 10. | _____   |
| 11. Enter the total of any amounts reported to the estate or trust on a Schedule K-1, Form 1099-DIV, or Form 2439 as "unrecaptured section 1250 gain" from an estate, trust, real estate investment trust, or mutual fund (or other regulated investment company) . . . . .   | 11. | _____   |
| 12. Enter the total of any unrecaptured section 1250 gain from sales (including installment sales) or other dispositions of section 1250 property held more than 1 year for which you did not make an entry in Part I of Form 4797 for the year of sale (see instructions) . . . . .  | 12. | _____   |
| 13. Add lines 9 through 12 . . . . .  | 13. | _____   |
| 14. If the estate or trust had any section 1202 gain or collectibles gain or (loss), enter the total of lines 1 through 4 of the <b>28% Rate Gain Worksheet</b> on page 35. Otherwise, enter -0- . . . . .  | 14. | _____   |
| 15. Enter the (loss), if any, from Schedule D, line 5b. If Schedule D, line 5b, is zero or a gain, enter -0- . . . . .  | 15. | (_____) |
| 16. Enter the estate's or trust's long-term capital loss carryovers from Schedule D, line 11, and from Schedule K-1 (Form 1041), line 13c, from another estate or trust . . . .   | 16. | (_____) |
| 17. Combine lines 14 through 16. If the result is a (loss), enter it as a positive amount. If the result is zero or a gain, enter -0- . . . . .   | 17. | _____   |
| 18. <b>Unrecaptured section 1250 gain.</b> Subtract line 17 from line 13. If zero or less, enter -0-. Enter the result here and in the appropriate columns of Schedule D, line 15d . . . . .  | 18. | _____   |

4797 (or the comparable line of Form 4797 for the year of sale) for that property. The result is the total unrecaptured section 1250 gain that must be allocated to the installment payments received from the sale.

**Step 3.** Generally, the amount of section 1231 gain on each installment payment is treated as unrecaptured section 1250 gain until the total unrecaptured section 1250 gain figured in step 2 has been used in full. Figure the amount of gain treated as unrecaptured section 1250 gain for installment payments received during the tax year, as the **smaller** of (a) the amount from line 26 or line 37 of the 2003 Form 6252, whichever applies, or (b) the amount of unrecaptured section 1250 gain remaining to be reported. This amount is generally the total unrecaptured section 1250 gain for the sale reduced by all gain reported in prior years (excluding section 1250 ordinary income recapture). However, if you chose not to treat all of the gain from payments received after May 6, 1997, and before August 24, 1999, as unrecaptured section 1250 gain, use only the amount you chose to treat as unrecaptured section 1250 gain for those payments to reduce the total unrecaptured section 1250 gain remaining to be reported for the sale. Include this amount on line 4.

**Line 10.** Include on line 10 the estate's or trust's share of the partnership's unrecaptured section 1250 gain that would result if the partnership had transferred all of its section 1250 property in a fully taxable transaction immediately before the estate or trust sold or exchanged its interest in that partnership. If the estate or trust recognized less than all of the realized gain, the partnership will be treated as having transferred only a proportionate amount of each section 1250 property.

**Line 12.** An example of an amount to include on line 12 is unrecaptured section 1250 gain from the sale of a vacation home previously used as a rental property but converted to personal use prior to the

sale. To figure the amount to enter on line 12, follow the applicable instructions below.

**Installment sales.** To figure the amount to include on line 12, follow the steps below for each installment sale of property held more than 1 year for which you did not make an entry in Part I of Form 4797 for the year of sale.

- **Step 1.** Figure the **smaller** of (a) the depreciation allowed or allowable or (b) the total gain for the sale. This is the **smaller** of line 22 or line 24 of the 2003 Form 4797 (or comparable lines of Form 4797 for the year of sale) for that property.

- **Step 2.** Reduce the amount figured in step 1 by any section 1250 ordinary income recapture for the sale. This is the amount from line 26g of the 2003 Form 4797 (or the comparable line of Form 4797 for the year of sale) for that property. The result is the total unrecaptured section 1250 gain that must be allocated to the installment payments received from the sale.

- **Step 3.** Generally, the amount of capital gain on each installment payment is treated as unrecaptured section 1250 gain until the total unrecaptured section 1250 gain figured in **step 2** has been used in full. Figure the amount of gain treated as unrecaptured section 1250 gain for installment payments received during the tax year, as the **smaller** of (a) the amount from line 26 or line 37 of the 2003 Form 6252, whichever applies, or (b) the amount of unrecaptured section 1250 gain remaining to be reported. This amount is generally the total unrecaptured section 1250 gain for the sale reduced by all gain reported in prior years (excluding section 1250 ordinary income recapture). However, if you chose not to treat all of the gain from payments received after May 6, 1997, and before August 24, 1999, as unrecaptured section 1250 gain, use only the amount you chose to treat as unrecaptured section 1250 gain for those payments to reduce the total unrecaptured section 1250 gain

remaining to be reported for the sale. Include this amount on line 12.

**Other sales or dispositions of section 1250 property.** For each sale of property held more than 1 year (for which an entry was not made in Part I of Form 4797), figure the **smaller** of (a) the depreciation allowed or allowable or (b) the total gain for the sale. This is the **smaller** of line 22 or line 24 of Form 4797 for that property. Next, reduce that amount by any section 1250 ordinary income recapture for the sale. This is the amount from line 26g of Form 4797 for that property. The result is the total unrecaptured section 1250 gain for the sale. Include this amount on line 12.

**Line 15e—28% Rate Gain or (Loss)**

Complete the 28% Rate Gain Worksheet if lines 15a and 16a for column (3) are both greater than zero and at least one of the following apply:

- The estate or trust reports in Part II, column (f), a section 1202 exclusion from the eligible gain on qualified small business stock (see page 31) or
- The estate or trust reports in Part II, column (f), a collectibles gain or (loss).

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

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

**Part IV—Capital Loss Limitation**

If the sum of all the capital losses is more than the sum of all the capital gains, then

**28% Rate Gain Worksheet—Line 15e**

*Keep for Your Records*

|   |              |
|---|--------------|
| 1. Enter the total of all collectibles gain or (loss) from items reported on line 6, column (f), of Schedule D  | 1. _____     |
| 2. Enter as a positive number the amount of any section 1202 exclusion reported on line 6, column (f), of Schedule D  | 2. _____     |
| 3. Enter the total of all collectibles gain or (loss) from Form 4684, line 4 (but only if Form 4684, line 15, is more than zero); Form 6252; Form 6781, Part II; and Form 8824  | 3. _____     |
| 4. Enter the total of any collectibles gain reported to the estate or trust on: <ul style="list-style-type: none"> <li>• Form 1099-DIV, box 2f;</li> <li>• Form 2439, box 1f; and</li> <li>• Schedule K-1 from a partnership, S corporation, estate, or trust.</li> </ul> | 4. _____     |
| 5. Enter the estate's or trust's long-term capital loss carryovers from Schedule D, line 11, and from line 13c of Schedule K-1 (Form 1041) from another estate or trust   | 5. ( _____ ) |
| 6. If Schedule D, line 5b, is a (loss), enter that (loss) here. Otherwise, enter -0-  | 6. ( _____ ) |
| 7. Combine lines 1 through 6. If zero or less, enter -0-. If more than zero, also enter this amount in the appropriate columns of Schedule D, line 15e  | 7. _____     |

Use this worksheet to figure the estate's or trust's capital loss carryovers from 2003 to 2004 if Schedule D, line 17, is a loss and **(a)** the loss on Schedule D, line 16a, col. (3), is more than \$3,000 or **(b)** Form 1041, page 1, line 22, is a loss.



|  |           |
|--|-----------|
| 1. Enter taxable income (or loss) from Form 1041, line 22  | 1. _____  |
| 2. Enter the loss from line 17 of Schedule D as a positive amount  | 2. _____  |
| 3. Enter amount from Form 1041, line 20  | 3. _____  |
| 4. Adjusted taxable income. Combine lines 1, 2, and 3. If zero or less, enter -0-  | 4. _____  |
| 5. Enter the <b>smaller</b> of line 2 or line 4  | 5. _____  |
| <b>Note:</b> If line 5b of Schedule D is a loss, go to line 6; otherwise, enter -0- on line 6 and go to line 10.   |           |
| 6. Enter loss from Schedule D, line 5b, as a positive amount   | 6. _____  |
| 7. Enter gain, if any, from Schedule D, line 13. If that line is blank or shows a loss, enter -0-  | 7. _____  |
| 8. Add lines 5 and 7   | 8. _____  |
| 9. <b>Short-term capital loss carryover to 2004.</b> Subtract line 8 from line 6. If zero or less, enter -0-. If this is the final return of the estate or trust, also enter on Schedule K-1 (Form 1041), line 13b   | 9. _____  |
| <b>Note:</b> If line 13 of Schedule D is a loss, go to line 10; otherwise, skip lines 10 through 14.   |           |
| 10. Enter loss from Schedule D, line 13, as a positive amount  | 10. _____ |
| 11. Enter gain, if any, from Schedule D, line 5b. If that line is blank or shows a loss, enter -0-   | 11. _____ |
| 12. Subtract line 6 from line 5. If zero or less, enter -0-  | 12. _____ |
| 13. Add lines 11 and 12  | 13. _____ |
| 14. <b>Long-term capital loss carryover to 2004.</b> Subtract line 13 from line 10. If zero or less, enter -0-. If this is the final return of the estate or trust, also enter on Schedule K-1 (Form 1041), line 13c | 14. _____ |

these capital losses are allowed as a deduction only to the extent of the smaller of the net loss or \$3,000.

For any year (including the final year) in which capital losses exceed capital gains, the estate or trust may have a capital loss carryover. Use the **Capital Loss Carryover Worksheet** (above) to figure any capital loss carryover. A capital loss carryover may be carried forward indefinitely. Capital losses keep their character as either short-term or long-term when carried over to the following year.

**Part V—Tax Computation Using Maximum Capital Gains Rates**

**Line 19**

If the estate or trust received capital gains or qualified dividends that were derived from income in respect of a decedent, you must reduce the amount on line 19 by the portion of the estate tax deduction claimed on Form 1041, page 1, line 19, that is attributable to the amount on Schedule D, line 19.

**Lines 28 and 40**

If the estate or trust files **Form 4952**, Investment Interest Expense Deduction, and the amount on line 4g is greater than the amount on line 4e of that form, use the worksheet below to figure the amount to enter on Schedule D, lines 28 and 40. Otherwise, enter on those lines the sum of lines 16b and 20 of Schedule D (unless you are skipping the line).

**Line 50**

If the tax using the maximum capital gains rates is less than the regular tax, enter the amount from line 50 on line 1a of Schedule G, Form 1041.

**Schedule D Tax Worksheet**

If you completed the Schedule D Tax Worksheet instead of Part V of Schedule D, be sure to enter the amount from line 51 of the worksheet on line 1a of Schedule G, Form 1041.

**Worksheet for Lines 28 and 40**

|  |          |
|--|----------|
| 1. Enter the estate's or trust's qualified dividends from Form 1041, line 2b(2)  | 1. _____ |
| 2. Enter the amount from Form 4952, line 4g  | 2. _____ |
| 3. Enter the amount from Form 4952, line 4e (or, if applicable, the smaller amount entered on the dotted line next to line 4e) | 3. _____ |
| 4. Subtract line 3 from line 2. If zero or less, enter -0-   | 4. _____ |
| 5. Subtract line 4 from line 1. If zero or less, enter -0-   | 5. _____ |
| 6. Enter the amount from Schedule D, line 16b  | 6. _____ |
| 7. Add lines 5 and 6. Enter the result here and on Schedule D, lines 28 and 40 (unless you are skipping the line)              | 7. _____ |

**Schedule D Tax Worksheet**

Keep for Your Records

**Complete this worksheet only if line 15d, column (2), or line 15e, column (2), of Schedule D is more than zero.**

**Exception:** Do not use this worksheet to figure the estate's or trust's tax if line 15a, column (2), or line 16a, column (2), of Schedule D or Form 1041, line 22, is zero or less; instead, see the instructions for Schedule G, line 1a of Form 1041.

|  |       |       |
|--|-------|-------|
| 1. Enter the estate's or trust's taxable income from Form 1041, line 22  | 1.    | _____ |
| 2. Enter qualified dividends, if any, from Form 1041, line 2b(2)   | 2.    | _____ |
| 3. Enter the amount from Form 4952, line 4g  | 3.    | _____ |
| 4. Enter the amount from Form 4952, line 4e*   | 4.    | _____ |
| 5. Subtract line 4 from line 3. If zero or less, enter -0-   | 5.    | _____ |
| 6. Subtract line 5 from line 2. If zero or less, enter -0-   | 6.    | _____ |
| 7. Enter the <b>smaller</b> of line 15a, col. (2) or line 16a, col. (2) from Sch. D  | 7.    | _____ |
| 8. Enter the <b>smaller</b> of line 3 or line 4  | 8.    | _____ |
| 9. Subtract line 8 from line 7. If zero or less, enter -0-   | 9.    | _____ |
| 10. Add lines 6 and 9  | 10.   | _____ |
| 11. Add lines 15d, column (2) and 15e, column (2) from Schedule D  | 11.   | _____ |
| 12. Enter the <b>smaller</b> of line 9 or line 11  | 12.   | _____ |
| 13. Subtract line 12 from line 10.   | 13.   | _____ |
| 14. Subtract line 13 from line 1. If zero or less, enter -0-   | 14.   | _____ |
| 15. Enter the <b>smaller</b> of line 1 or \$1,900  | 15.   | _____ |
| 16. Enter the <b>smaller</b> of line 14 or line 15   | 16.   | _____ |
| 17. Subtract line 10 from line 1. If zero or less, enter -0-   | 17.   | _____ |
| 18. Enter the <b>larger</b> of line 16 or line 17  | ▶ 18. | _____ |
| <b>If lines 15 and 16 are the same, skip lines 19 through 28 and go to line 29. Otherwise, go to line 19.</b>  |       |       |
| 19. Subtract line 16 from line 15  | ▶ 19. | _____ |
| 20. Add line 16b, column (2) (from Schedule D) and line 6 (above)  | 20.   | _____ |
| 21. Enter the <b>smaller</b> of line 19 or line 20   | 21.   | _____ |
| 22. Multiply line 21 by 5% (.05)   | 22.   | _____ |
| <b>If lines 19 and 21 are the same, skip lines 23 through 28 and go to line 29. Otherwise, go to line 23.</b>  |       |       |
| 23. Subtract line 21 from line 19  | 23.   | _____ |
| 24. Enter the estate's or trust's allocable portion of qualified 5-year gain, if any, from Schedule D, line 15c, column (2)  | 24.   | _____ |
| 25. Enter the <b>smaller</b> of line 23 or line 24   | 25.   | _____ |
| 26. Multiply line 25 by 8% (.08)   | 26.   | _____ |
| 27. Subtract line 25 from line 23  | 27.   | _____ |
| 28. Multiply line 27 by 10% (.10)  | 28.   | _____ |
| <b>If lines 1 and 15 are the same, skip lines 29 through 47 and go to line 48. Otherwise, go to line 29.</b>   |       |       |
| 29. Enter the <b>smaller</b> of line 1 or line 13  | 29.   | _____ |
| 30. Enter the amount from line 19 (if line 19 is blank, enter -0-)   | 30.   | _____ |
| 31. Subtract line 30 from line 29. If zero or less, enter -0-  | ▶ 31. | _____ |
| 32. Add line 16b, column (2) (from Schedule D) and line 6 (above)  | 32.   | _____ |
| 33. Enter the amount from line 21 (if line 21 is blank, enter -0-)   | 33.   | _____ |
| 34. Subtract line 33 from line 32  | 34.   | _____ |
| 35. Enter the <b>smaller</b> of line 31 or line 34   | 35.   | _____ |
| 36. Multiply line 35 by 15% (.15)  | 36.   | _____ |
| 37. Subtract line 35 from line 31  | 37.   | _____ |
| 38. Multiply line 37 by 20% (.20)  | 38.   | _____ |
| <b>If Schedule D, line 15d, column (2) is zero or blank, skip lines 39 through 44 and go to line 45. Otherwise, go to line 39.</b>   |       |       |
| 39. Enter the <b>smaller</b> of line 9 (above) or line 15d, col. (2) (from Schedule D)   | 39.   | _____ |
| 40. Add lines 10 and 18  | 40.   | _____ |
| 41. Enter the amount from line 1 above   | 41.   | _____ |
| 42. Subtract line 41 from line 40. If zero or less, enter -0-  | 42.   | _____ |
| 43. Subtract line 42 from line 39. If zero or less, enter -0-  | ▶ 43. | _____ |
| 44. Multiply line 43 by 25% (.25)  | 44.   | _____ |
| <b>If Schedule D, line 15e, column (2) is zero or blank, skip lines 45 through 47 and go to line 48. Otherwise, go to line 45.</b>   |       |       |
| 45. Add lines 18, 19, 31, and 43   | 45.   | _____ |
| 46. Subtract line 45 from line 1   | 46.   | _____ |
| 47. Multiply line 46 by 28% (.28)  | 47.   | _____ |
| 48. Figure the tax on the amount on <b>line 18</b> . Use the 2003 Tax Rate Schedule on page 21   | 48.   | _____ |
| 49. Add lines 22, 26, 28, 36, 38, 44, 47, and 48   | 49.   | _____ |
| 50. Figure the tax on the amount on <b>line 1</b> . Use 2003 Tax Rate Schedule on page 21  | 50.   | _____ |
| 51. <b>Tax on all taxable income (including capital gains and qualified dividends).</b> Enter the <b>smaller</b> of line 49 or line 50 here <b>and</b> on line 1a of Sch. G, Form 1041 | 51.   | _____ |

\*If applicable, enter instead the smaller amount entered on the dotted line next to line 4e of Form 4952.

# Schedule J (Form 1041) — Accumulation Distribution for Certain Complex Trusts

## General Instructions

Use Schedule J (Form 1041) to report an accumulation distribution for a domestic complex trust that was:

- Previously treated at any time as a foreign trust (unless an exception is provided in future regulations) or
- Created before March 1, 1984, unless that trust would not be aggregated with other trusts under the rules of section 643(f) if that section applied to the trust.

An accumulation distribution is the excess of amounts properly paid, credited, or required to be distributed (other than income required to be distributed currently) over the DNI of the trust reduced by income required to be distributed currently. To have an accumulation distribution, the distribution must exceed the accounting income of the trust.

## Specific Instructions

### Part I—Accumulation Distribution in 2003

#### Line 1—Distribution Under Section 661(a)(2)

Enter the amount from Schedule B of Form 1041, line 10, for 2003. This is the amount properly paid, credited, or required to be distributed other than the amount of income for the current tax year required to be distributed currently.

#### Line 2—Distributable Net Income

Enter the amount from Schedule B of Form 1041, line 7, for 2003. This is the amount of distributable net income (DNI) for the current tax year determined under section 643(a).

#### Line 3—Distribution Under Section 661(a)(1)

Enter the amount from Schedule B of Form 1041, line 9, for 2003. This is the amount of income for the current tax year required to be distributed currently.

#### Line 5—Accumulation Distribution

If line 11, Schedule B of Form 1041 is more than line 8, Schedule B of Form 1041, complete the rest of Schedule J and file it with Form 1041, unless the trust has no previously accumulated income.

Generally, amounts accumulated before a beneficiary reaches age 21 may be excluded by the beneficiary. See sections 665 and 667(c) for exceptions relating to multiple trusts. The trustee reports to the IRS the total amount of the accumulation distribution before any reduction for income accumulated before the beneficiary reaches age 21. If the multiple trust rules do not apply, the beneficiary claims the exclusion when filing **Form 4970**, Tax on Accumulation

Distribution of Trusts, as you may not be aware that the beneficiary may be a beneficiary of other trusts with other trustees.

For examples of accumulation distributions that include payments from one trust to another trust, and amounts distributed for a dependent's support, see Regulations section 1.665(b)-1A(b).

## Part II—Ordinary Income Accumulation Distribution

Enter the applicable year at the top of each column for each throwback year.

### Line 6—Distributable Net Income for Earlier Years

Enter the applicable amounts as follows:

| Throwback year(s)   | Amount from line              |
|---------------------|-------------------------------|
| 1969–1977 . . . . . | Schedule C, Form 1041, line 5 |
| 1978–1979 . . . . . | Form 1041, line 61            |
| 1980 . . . . .      | Form 1041, line 60            |
| 1981–1982 . . . . . | Form 1041, line 58            |
| 1983–1996 . . . . . | Schedule B, Form 1041, line 9 |
| 1997–2002 . . . . . | Schedule B, Form 1041, line 7 |

For information about throwback years, see the instructions for line 13. For purposes of line 6, in figuring the DNI of the trust for a throwback year, subtract any estate tax deduction for income in respect of a decedent if the income is includible in figuring the DNI of the trust for that year.

### Line 7—Distributions Made During Earlier Years

Enter the applicable amounts as follows:

| Throwback year(s)   | Amount from line               |
|---------------------|--------------------------------|
| 1969–1977 . . . . . | Schedule C, Form 1041, line 8  |
| 1978 . . . . .      | Form 1041, line 64             |
| 1979 . . . . .      | Form 1041, line 65             |
| 1980 . . . . .      | Form 1041, line 64             |
| 1981–1982 . . . . . | Form 1041, line 62             |
| 1983–1996 . . . . . | Schedule B, Form 1041, line 13 |
| 1997–2002 . . . . . | Schedule B, Form 1041, line 11 |

### Line 11—Prior Accumulation Distribution Thrown Back to any Throwback Year

Enter the amount of prior accumulation distributions thrown back to the throwback years. Do not enter distributions excluded under section 663(a)(1) for gifts, bequests, etc.

### Line 13—Throwback Years

Allocate the amount on line 5 that is an accumulation distribution to the earliest applicable year first, but do not allocate more than the amount on line 12 for any throwback year. An accumulation distribution is thrown back first to the earliest preceding tax year in which there is undistributed net income (UNI). Then, it is thrown back beginning with the next earliest year to any remaining preceding tax years of the trust. The portion of the accumulation distribution allocated to the earliest preceding tax year is the amount of the UNI for that year. The portion of the accumulation distribution allocated to any remaining preceding tax year is the

amount by which the accumulation distribution is larger than the total of the UNI for all earlier preceding tax years.

A tax year of a trust during which the trust was a simple trust for the entire year is not a preceding tax year unless (a) during that year the trust received outside income or (b) the trustee did not distribute all of the trust's income that was required to be distributed currently for that year. In this case, UNI for that year must not be more than the greater of the outside income or income not distributed during that year.

The term "outside income" means amounts that are included in the DNI of the trust for that year but that are not "income" of the trust as defined in Regulations section 1.643(b)-1. Some examples of outside income are: (a) income taxable to the trust under section 691; (b) unrealized accounts receivable that were assigned to the trust; and (c) distributions from another trust that include the DNI or UNI of the other trust.

### Line 16—Tax-Exempt Interest Included on Line 13

For each throwback year, divide line 15 by line 6 and multiply the result by the following:

| Throwback year(s)   | Amount from line                 |
|---------------------|----------------------------------|
| 1969–1977 . . . . . | Schedule C, Form 1041, line 2(a) |
| 1978–1979 . . . . . | Form 1041, line 58(a)            |
| 1980 . . . . .      | Form 1041, line 57(a)            |
| 1981–1982 . . . . . | Form 1041, line 55(a)            |
| 1983–2002 . . . . . | Schedule B, Form 1041, line 2    |

## Part III—Taxes Imposed on Undistributed Net Income

For the regular tax computation, if there is a capital gain, complete lines 18 through 25 for each throwback year. If the trustee elected the alternative tax on capital gains, complete lines 26 through 31 instead of lines 18 through 25 for each applicable year. If there is no capital gain for any year, or there is a capital loss for every year, enter on line 9 the amount of the tax for each year identified in the instruction for line 18 and do not complete Part III. If the trust received an accumulation distribution from another trust, see Regulations section 1.665(b)-1A.

**Note:** *The alternative tax on capital gains was repealed for tax years beginning after December 31, 1978. The maximum rate on net capital gain for 1981, 1987, and 1991 through 2002 is not an alternative tax for this purpose.*

### Line 18—Regular Tax

Enter the applicable amounts as follows:

| Throwback year(s)   | Amount from line               |
|---------------------|--------------------------------|
| 1969–1976 . . . . . | Form 1041, page 1, line 24     |
| 1977 . . . . .      | Form 1041, page 1, line 26     |
| 1978–1979 . . . . . | Form 1041, line 27             |
| 1980–1984 . . . . . | Form 1041, line 26c            |
| 1985–1986 . . . . . | Form 1041, line 25c            |
| 1987 . . . . .      | Form 1041, line 22c            |
| 1988–2002 . . . . . | Schedule G, Form 1041, line 1a |

## Line 19—Trust's Share of Net Short-Term Gain

For each throwback year, enter the smaller of the capital gain from the two lines indicated. If there is a capital loss or a zero on either or both of the two lines indicated, enter zero on line 19.

| Throwback year(s) | Amount from line  |
|-------------------|---|
| 1969–1970         | Schedule D, line 10, column 2, or Schedule D, line 12, column 2     |
| 1971–1978         | Schedule D, line 14, column 2, or Schedule D, line 16, column 2     |
| 1979              | Schedule D, line 18, column (b), or Schedule D, line 20, column (b) |
| 1980–1981         | Schedule D, line 14, column (b), or Schedule D, line 16, column (b) |
| 1982              | Schedule D, line 16, column (b), or Schedule D, line 18, column (b) |
| 1983–1996         | Schedule D, line 15, column (b), or Schedule D, line 17, column (b) |
| 1997–2002         | Schedule D, line 14, column (2), or Schedule D, line 16, column (2) |

## Line 20—Trust's Share of Net Long-Term Gain

Enter the applicable amounts as follows:

| Throwback year(s) | Amount from line   |
|-------------------|--|
| 1969–1970         | 50% of Schedule D, line 13(e)  |
| 1971–1977         | 50% of Schedule D, line 17(e)  |
| 1978              | Schedule D, line 17(e), or line 31, whichever is applicable, less Form 1041, line 23 |
| 1979              | Schedule D, line 25 or line 27, whichever is applicable, less Form 1041, line 23     |
| 1980–1981         | Schedule D, line 21, less Schedule D, line 22  |
| 1982              | Schedule D, line 23, less Schedule D, line 24  |
| 1983–1986         | Schedule D, line 22, less Schedule D, line 23  |
| 1987–1996         | Schedule D, the smaller of any gain on line 16 or line 17, column (b)                |
| 1997–2001         | Schedule D, the smaller of any gain on line 15c or line 16, column (2)               |
| 2002              | Schedule D, the smaller of any gain on line 15a or line 16, column (2)               |

## Line 22—Taxable Income

Enter the applicable amounts as follows:

| Throwback year(s) | Amount from line           |
|-------------------|----------------------------|
| 1969–1976         | Form 1041, page 1, line 23 |
| 1977              | Form 1041, page 1, line 25 |
| 1978–1979         | Form 1041, line 26         |

|           |                    |
|-----------|--------------------|
| 1980–1984 | Form 1041, line 25 |
| 1985–1986 | Form 1041, line 24 |
| 1987      | Form 1041, line 21 |
| 1988–1996 | Form 1041, line 22 |
| 1997      | Form 1041, line 23 |
| 1998–2002 | Form 1041, line 22 |

## Line 26—Tax on Income Other Than Long-Term Capital Gain

Enter the applicable amounts as follows:

| Throwback year(s) | Amount from line    |
|-------------------|---------------------|
| 1969              | Schedule D, line 20 |
| 1970              | Schedule D, line 19 |
| 1971              | Schedule D, line 50 |
| 1972–1975         | Schedule D, line 48 |
| 1976–1978         | Schedule D, line 27 |

## Line 27—Trust's Share of Net Short-Term Gain

If there is a loss on any of the following lines, enter zero on line 27 for the applicable throwback year. Otherwise, enter the applicable amounts as follows:

| Throwback year(s) | Amount from line              |
|-------------------|-------------------------------|
| 1969–1970         | Schedule D, line 10, column 2 |
| 1971–1978         | Schedule D, line 14, column 2 |

## Line 28—Trust's Share of Taxable Income Less Section 1202 Deduction

Enter the applicable amounts as follows:

| Throwback year(s) | Amount from line    |
|-------------------|---------------------|
| 1969              | Schedule D, line 19 |
| 1970              | Schedule D, line 18 |
| 1971              | Schedule D, line 38 |
| 1972–1975         | Schedule D, line 39 |
| 1976–1978         | Schedule D, line 21 |

## Part IV—Allocation to Beneficiary

Complete Part IV for each beneficiary. If the accumulation distribution is allocated to more than one beneficiary, attach an additional copy of Schedule J with Part IV completed for each additional beneficiary. Give each beneficiary a copy of his or her respective Part IV information. If more than 5 throwback years are involved, use another Schedule J, completing Parts II and III for each additional throwback year.

If the beneficiary is a nonresident alien individual or a foreign corporation, see section 667(e) about retaining the character of the amounts distributed to determine the amount of the U.S. withholding tax.

The beneficiary uses Form 4970 to figure the tax on the distribution. The beneficiary also uses Form 4970 for the section 667(b)(6) tax adjustment if an accumulation distribution is subject to estate or generation-skipping transfer tax. This is because the trustee may not be the estate or generation-skipping transfer tax return filer.

## Schedule K-1 (Form 1041)—Beneficiary's Share of Income, Deductions, Credits, etc.

### A Change To Note

We have added new lines to account for the reduction in the tax rates for capital gains and qualified dividends.

### General Instructions

Use Schedule K-1 (Form 1041) to report the beneficiary's share of income, deductions, and credits from a trust or a decedent's estate.



**Grantor type trusts do not use Schedule K-1 (Form 1041) to report the income, deductions, or credits of the grantor (or other person treated as owner). See *Special Filing Instructions for Grantor Type Trusts, Pooled Income Funds, and Electing Small Business Trusts* on page 5.**

### Who Must File

The fiduciary (or one of the joint fiduciaries) must file Schedule K-1. A copy of each beneficiary's Schedule K-1 is attached to the Form 1041 filed with the IRS and each beneficiary is given a copy of his or her respective Schedule K-1. One copy of each Schedule K-1 must be retained for the fiduciary's records.

### Beneficiary's Identifying Number

As a payer of income, you are required under section 6109 to request and provide a proper identifying number for each recipient of income. Enter the beneficiary's number on the respective Schedule K-1 when you file Form 1041. Individuals and business recipients are responsible for giving you their TIN upon request. You may use **Form W-9, Request for Taxpayer Identification Number and Certification**, to request the beneficiary's identifying number.

**Penalty.** Under section 6723, the payer is charged a \$50 penalty for each failure to provide a required TIN, unless reasonable cause is established for not providing it. Explain any reasonable cause in a signed affidavit and attach it to this return.

### Tax Shelter's Identification Number

If the estate or trust is a tax shelter, is involved in a tax shelter, or is considered to be the organizer of a tax shelter, there are reporting requirements under section 6111 for both the fiduciaries and the beneficiaries.

See **Form 8264, Application for Registration of a Tax Shelter**, and **Form 8271, Investor Reporting of Tax Shelter Registration Number**, and their related instructions for information regarding the fiduciary's reporting requirements.

### Substitute Forms

You do not need prior IRS approval for a substitute Schedule K-1 (Form 1041) that

follows the specifications for filing substitute Schedules K-1 in **Pub. 1167**, General Rules and Specifications for Substitute Forms and Schedules, or is an exact copy of an IRS Schedule K-1. You must request IRS approval to use other substitute Schedules K-1. To request approval, write to:

Internal Revenue Service  
Attention: Substitute Forms Program  
SE:W:CAR:MP:T:T:SP  
Rm. 6411  
1111 Constitution Avenue, NW  
Washington, DC 20224

## Inclusion of Amounts in Beneficiaries' Income

**Simple trust.** The beneficiary of a simple trust must include in his or her gross income the amount of the income required to be distributed currently, whether or not distributed, or if the income required to be distributed currently to all beneficiaries exceeds the distributable net income (DNI), his or her proportionate share of the DNI. The determination of whether trust income is required to be distributed currently depends on the terms of the trust instrument and applicable local law. See Regulations section 1.652(c)-4 for a comprehensive example.

**Estates and complex trusts.** The beneficiary of a decedent's estate or complex trust must include in his or her gross income the sum of:

1. The amount of the income required to be distributed currently, or if the income required to be distributed currently to all beneficiaries exceeds the DNI (figured without taking into account the charitable deduction), his or her proportionate share of the DNI (as so figured) and

2. All other amounts properly paid, credited, or required to be distributed, or if the sum of the income required to be distributed currently and other amounts properly paid, credited, or required to be distributed to all beneficiaries exceeds the DNI, his or her proportionate share of the excess of DNI over the income required to be distributed currently.

See Regulations section 1.662(c)-4 for a comprehensive example.

For complex trusts that have more than one beneficiary, and if different beneficiaries have substantially separate and independent shares, their shares are treated as separate trusts for the sole purpose of determining the amount of DNI allocable to the respective beneficiaries. For the estates of decedents dying after August 5, 1997, a similar rule applies to treat substantially separate and independent shares of different beneficiaries of an estate as separate estates. For examples of the application of the separate share rule, see the regulations under section 663(c).

**Character of income.** The beneficiary's income is considered to have the same proportion of each class of items entering

into the computation of DNI that the total of each class has to the DNI (e.g., half dividends and half interest if the income of the estate or trust is half dividends and half interest).

**Allocation of deductions.** Generally, items of deduction that enter into the computation of DNI are allocated among the items of income to the extent such allocation is not inconsistent with the rules set out in section 469 and its regulations, relating to passive activity loss limitations, in the following order.

First, all deductions directly attributable to a specific class of income are deducted from that income. For example, rental expenses, to the extent allowable, are deducted from rental income.

Second, deductions that are not directly attributable to a specific class of income generally may be allocated to any class of income, as long as a reasonable portion is allocated to any tax-exempt income. Deductions considered not directly attributable to a specific class of income under this rule include fiduciary fees, safe deposit box rental charges, and state income and personal property taxes. The charitable deduction, however, must be ratably apportioned among each class of income included in DNI.

Finally, any excess deductions that are directly attributable to a class of income may be allocated to another class of income. However, in no case can excess deductions from a passive activity be allocated to income from a nonpassive activity, or to portfolio income earned by the estate or trust. Excess deductions attributable to tax-exempt income cannot offset any other class of income.

In no case can deductions be allocated to an item of income that is not included in the computation of DNI, or attributable to corpus.

Except for the final year, and for depreciation or depletion allocations in excess of income (see Rev. Rul. 74-530, 1974-2 C.B. 188), you may not show any negative amounts for any class of income, because the beneficiary generally may not claim losses or deductions from the estate or trust.

**Gifts and bequests.** Do not include in the beneficiary's income any gifts or bequests of a specific sum of money or of specific property under the terms of the governing instrument that are paid or credited in three installments or less.

Amounts that can be paid or credited only from income of the estate or trust do not qualify as a gift or bequest of a specific sum of money.

**Past years.** Do not include in the beneficiary's income any amounts deducted on Form 1041 for an earlier year that were credited or required to be distributed in that earlier year.

## Beneficiary's Tax Year

The beneficiary's income from the estate or trust must be included in the

beneficiary's tax year during which the tax year of the estate or trust ends. See Pub. 559 for more information, including the effect of the death of a beneficiary during the tax year of the estate or trust.

## Specific Instructions

### Line 1—Interest

Enter the beneficiary's share of the taxable interest income minus allocable deductions.

### Line 2b—Total Ordinary Dividends

Enter the beneficiary's share of ordinary dividends minus allocable deductions.

### Line 3a—Net Short-Term Capital Gain

Enter the beneficiary's share of the net short-term capital gain from line 14a, column (1), Schedule D (Form 1041), minus allocable deductions. Do not enter a loss on line 3a. If, for the final year of the estate or trust, there is a capital loss carryover, enter on line 13b the beneficiary's share of short-term capital loss carryover. However, if the beneficiary is a corporation, enter on line 13b the beneficiary's share of all short- and long-term capital loss carryovers as a single item. See section 642(h) and related regulations for more information.

### Line 3b—Net Short-Term Capital Gain (Post 5/5/2003)

If you entered an amount on line 3a (above), enter the beneficiary's share of line 14b(1), if any, from Schedule D minus any allocable deductions used on line 3a (above).

### Lines 4a through 4e—Net Long-Term Capital Gain

Enter the beneficiary's share of the net long-term capital gain from lines 15a through 15e, column (1), Schedule D (Form 1041) minus allocable deductions.

**Do not** enter a loss on lines 4a through 4e. If, for the final year of the estate or trust, there is a capital loss carryover, enter on line 13c the beneficiary's share of the long-term capital loss carryover. (If the beneficiary is a corporation, see the instructions for line 3a.) See section 642(h) and related regulations for more information.

Gains or losses from the complete or partial disposition of a rental, rental real estate, or trade or business activity that is a passive activity, must be shown on an attachment to Schedule K-1.

### Line 5a—Annuities, Royalties, and Other Nonpassive Income

Enter the beneficiary's share of annuities, royalties, or any other income, minus allocable deductions (other than directly apportionable deductions), that is **not** subject to any passive activity loss limitation rules at the beneficiary level. Use line 6a to report income items subject to the passive activity rules at the beneficiary's level.



## Lines 5b and 6b—Depreciation

Enter the beneficiary's share of the depreciation deductions attributable to each activity reported on lines 5a and 6a. See the instructions on page 15 for a discussion of how the depreciation deduction is apportioned between the beneficiaries and the estate or trust. Report any AMT adjustment or tax preference item attributable to depreciation separately on line 12a.

**Note:** *An estate or trust cannot make an election under section 179 to expense certain tangible property.*

## Lines 5c and 6c—Depletion

Enter the beneficiary's share of the depletion deduction under section 611 attributable to each activity reported on lines 5a and 6a. See the instructions on page 15 for a discussion of how the depletion deduction is apportioned between the beneficiaries and the estate or trust. Report any tax preference item attributable to depletion separately on line 12b.

## Lines 5d and 6d—Amortization

Itemize the beneficiary's share of the amortization deductions attributable to each activity reported on lines 5a and 6a. Apportion the amortization deductions between the estate or trust and the beneficiaries in the same way that the depreciation and depletion deductions are divided. Report any AMT adjustment attributable to amortization separately on line 12c.

## Line 6a—Trade or Business, Rental Real Estate, and Other Rental Income

Enter the beneficiary's share of trade or business, rental real estate, and other rental income, minus allocable deductions (other than directly apportionable deductions). To assist the beneficiary in figuring any applicable passive activity loss limitations, also attach a separate schedule showing the beneficiary's share of income derived from each trade or business, rental real estate, and other rental activity.

## Lines 6b Through 6d



*The limitations on passive activity losses and credits under section 469 apply to estates and trusts. Estates and trusts that distribute income to beneficiaries are allowed to apportion depreciation, depletion, and amortization deductions to the beneficiaries. These deductions are referred to as "directly apportionable deductions."*

*Rules for treating a beneficiary's income and directly apportionable deductions from an estate or trust and other rules for applying the passive loss and credit limitations to beneficiaries of estates and trusts have not yet been issued.*

Any directly apportionable deduction, such as depreciation, is treated by the beneficiary as having been incurred in the

same activity as incurred by the estate or trust. However, the character of such deduction may be determined as if the beneficiary incurred the deduction directly.

To assist the beneficiary in figuring any applicable passive activity loss limitations, also attach a separate schedule showing the beneficiary's share of directly apportionable deductions derived from each trade or business, rental real estate, and other rental activity.

## Line 7—Income for Minimum Tax Purposes

Enter the beneficiary's share of the income distribution deduction figured on a minimum tax basis from line 44 of Schedule I.

## Line 8—Income for Regular Tax Purposes

Enter the beneficiary's share of the income distribution deduction figured on line 15 of Schedule B. This amount should equal the sum of lines 1, 2b, 3a, 4a, 5a, and 6a.

## Line 10—Estate Tax Deduction (Including Certain Generation-Skipping Transfer Taxes)

If the distribution deduction consists of any income in respect of a decedent, and the estate or trust was allowed a deduction under section 691(c) for the estate tax paid attributable to such income (see the line 19 instructions on page 18), then the beneficiary is allowed an estate tax deduction in proportion to his or her share of the distribution that consists of such income. For an example of the computation, see Regulations section 1.691(c)-2. Figure the computation on a separate sheet and attach it to the return.

## Line 11—Foreign Taxes

List on a separate sheet the beneficiary's share of the applicable foreign taxes paid or accrued and the various foreign source figures needed to figure the beneficiary's foreign tax credit. See Pub. 514 and section 901(b)(5) for special rules about foreign taxes.

## Lines 12a through 12c

Enter any adjustments or tax preference items attributable to depreciation, depletion, or amortization that were allocated to the beneficiary. For property placed in service before 1987, report separately the accelerated depreciation of real and leased personal property.

## Line 12d—Exclusion Items

Enter the beneficiary's share of the adjustment for minimum tax purposes from Schedule K-1, line 9, that is attributable to exclusion items (Schedule I, lines 2 through 6 and 8).

## Line 13a—Excess Deductions on Termination

If this is the final return of the estate or trust, and there are excess deductions on

termination (see the instructions for line 22 on page 17), enter the beneficiary's share of the excess deductions on line 13a. Figure the deductions on a separate sheet and attach it to the return.

Excess deductions on termination occur only during the last tax year of the trust or decedent's estate when the total deductions (excluding the charitable deduction and exemption) are greater than the gross income during that tax year.

Generally, a deduction based on an NOL carryover is not available to a beneficiary as an excess deduction. However, if the last tax year of the estate or trust is also the last year in which an NOL carryover may be taken (see section 172(b)), the NOL carryover is considered an excess deduction on the termination of the estate or trust to the extent it is not absorbed by the estate or trust during its final tax year. For more information, see Regulations section 1.642(h)-4 for a discussion of the allocation of the carryover among the beneficiaries.

Only the beneficiary of an estate or trust that succeeds to its property is allowed to deduct that entity's excess deductions on termination. A beneficiary who does not have enough income in that year to absorb the entire deduction may not carry the balance over to any succeeding year. An individual beneficiary must be able to itemize deductions in order to claim the excess deductions in determining taxable income.

## Lines 13b and 13c—Unused Capital Loss Carryover

Upon termination of the trust or decedent's estate, the beneficiary succeeding to the property is allowed as a deduction any unused capital loss carryover under section 1212. If the estate or trust incurs capital losses in the final year, use the **Capital Loss Carryover Worksheet** on page 36 to figure the amount of capital loss carryover to be allocated to the beneficiary.

## Lines 13d and 13e—Net Operating Loss (NOL) Carryover

Upon termination of a trust or decedent's estate, a beneficiary succeeding to its property is allowed to deduct any unused NOL (and any ATNOL) carryover for regular and AMT purposes if the carryover would be allowable to the estate or trust in a later tax year but for the termination. Enter on lines 13d and 13e the unused carryover amounts.

## Line 14—Other

Itemize on line 14, or on a separate sheet if more space is needed, the beneficiary's tax information not entered elsewhere on Schedule K-1. This includes any tax withheld on distributions to foreign persons. It also includes the allocable share, if any, of:

- Payment of estimated tax to be credited to the beneficiary (section 643(g));



See the instructions for line 24b on page 19 **before** you make an entry to allocate any estimated tax payments to a beneficiary.

- Tax-exempt interest income received or accrued by the trust (including exempt-interest dividends from a mutual fund or other regulated investment company);
- Investment income (section 163(d));
- Gross farming and fishing income;
- Credit for backup withholding (section 3406);
- The information a beneficiary will need to figure any investment credit;
- The work opportunity credit;
- The welfare-to-work credit;
- The alcohol fuel credit;
- The credit for increasing research activities;
- The low-income housing credit;
- The renewable electricity production credit;
- The empowerment zone and renewal community employment credit;
- The Indian employment credit;
- The orphan drug credit;
- Credit for employer-provided child care facilities and services;
- New York Liberty Zone business employee credit;
- The information a beneficiary will need to figure any recapture taxes; and
- Foreign trading gross receipts as defined in section 942(a).

**Note:** Upon termination of an estate or trust, any suspended passive activity losses (PALs) relating to an interest in a passive activity cannot be allocated to the beneficiary. Instead, the basis in such

activity is increased by the amount of any PALs allocable to the interest, and no losses are allowed as a deduction on the estate's or trust's final Form 1041.

**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.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete and file this form and related schedules will vary depending on individual circumstances. The estimated average times are:

|   | Form 1041       | Schedule D      | Schedule D Tax Worksheet | Schedule J      | Schedule K-1   |
|---|-----------------|-----------------|--------------------------|-----------------|----------------|
| <b>Recordkeeping</b>  | 54 hr., 44 min. | 33 hr., 12 min. | 12 hr., 12 min.          | 39 hr., 27 min. | 9 hr., 48 min. |
| <b>Learning about the law or the form</b>                   | 20 hr., 22 min. | 2 hr., 40 min.  | - - - -                  | 1 hr., 17 min.  | 1 hr., 23 min. |
| <b>Preparing the form</b>                                   | 37 hr., 57 min. | 3 hr., 17 min.  | 12 min.                  | 1 hr., 59 min.  | 1 hr., 36 min. |
| <b>Copying, assembling, and sending the form to the IRS</b> | 4 hr., 33 min.  | - - - -         | - - - -                  | - - - -         | - - - -        |

If you have comments concerning the accuracy of these time estimates or suggestions for making this form and related schedules simpler, we would be happy to hear from you. You can write to the Tax Products Coordinating Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **Do not** send the tax form to this address. Instead, see **Where To File** on page 44.



## Where To File

For all estates and trusts, including charitable and split-interest trusts and pooled income funds:

| IF you are located in ...  | THEN use this address if you:  |  |
|--|--|--|
|  | Are not enclosing a check or money order ...                           | Are enclosing a check or money order ...                               |
| Connecticut, Delaware, District of Columbia, Illinois, Indiana, Kentucky, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, West Virginia, Wisconsin                 | Internal Revenue Service Center, Cincinnati, Ohio 45999-0048           | Internal Revenue Service Center, Cincinnati, Ohio 45999-0148           |
| Alabama, Alaska, Arizona, Arkansas, California, Colorado, Florida, Georgia, Hawaii, Idaho, Iowa, Kansas, Louisiana, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Tennessee, Texas, Utah, Washington, Wyoming | Internal Revenue Service Center, Ogden, Utah 84201-0048                | Internal Revenue Service Center, Ogden, Utah 84201-0148                |
| A foreign country or a United States possession  | Internal Revenue Service Center, Philadelphia, Pennsylvania 19255-0048 | Internal Revenue Service Center, Philadelphia, Pennsylvania 19255-0148 |