Sale of a Primary Residence

Or simply, selling your home

Brenda Bloch-Young, July 2021

Recent WSJ article regarding the gain exclusion

Confusing? Might be….

- Prior to 1997, the gain on the sale of a principal residence was deferred if the home owners purchased a new home of equal or greater value.
- Note there were exceptions, but this was the basic concept.
- However, the gain was “deferred” and it reduced the cost basis of the new home.
- Under current law, a single taxpayer may exclude a $250k gain, married filing jointly taxpayer a $500k gain (plus widows and widowers within a time period.)
- Excess gains are taxed at capital gains tax rates

Gain exclusion

Of course, nothing is ever quite this simple

- To exclude a gain, the home must have been used as a primary residence for 2 of the last 5 years.
- Again, several nuanced variations of this and exceptions
- Best source of the details is the IRS Publication 523 (2020), Selling Your Home - https://www.irs.gov/publications/p523
- WSJ pointed out that there is a stepped up basis at death. A home owned jointly in a community property state like California would likely not have a gain if one spouse died prior to the sale. Note Virginia is not a community property state - the stepped up basis would apply to only half of a home owned jointly.

Unusual circumstances

Convert a vacation home to a primary residence?
Operated a business out of your home?

- Again, another set of rules.
- Sell the principal residence and move into the vacation home.
- The vacation home becomes the new primary residence
- It’s possible that only a portion of the gain may be excluded
- Business in your home? Another set of rules

Some new proposals from the Administration

Impacting high income taxpayers

WSJ - “Home sellers with gains exceeding those limits (exclusion amounts) who have annual income above $1 million <u>would owe a 43.4% rate</u> on the portion of their total long-term capital gains above $1 million. If income is less than $1 million, the top rate on the gains would apparently remain 23.8%. Under the current Biden proposal, these rates would apply to sales after late April, 2021.”

Determine the cost basis of your home

IRS Publication 523 has the answers

- The cost of the home plus costs incurred to purchase
- Capital improvements over the years
- Maintenance such as cleaning drains and painting do not add to the cost basis
- The IRS publication has multiple examples and lists

Deferred gain under the old rules may haunt you

Google this topic - Both the Washington Post and Turbo Tax have examples

- Theoretically, if you have owned multiple residences over the years and you continued to purchase a more expensive home, you may have differed gains that impact the cost basis of your current home.
- This rollover provision was in force through May 6, 1997. The Taxpayer Relief Act of 1997 abolished the rollover.
- A home purchased prior to the change in the law may have a lower cost basis than the purchase price as it must be adjusted for the gains deferred in the past.
- Old tax returns included Form 2119 that calculated the deferred gain roll-over.

Summary

Now is the time to determine your cost basis

1. Begin with gathering the records you have
2. Read the IRS Publication on Selling Your Home
3. Consult with a CPA or your tax preparer

Don’t leave this task to your spouse or your kids.