2007 Planning:
Exclusion of Gain on Sale of Principal Residence

If you anticipate selling your home in the near future, you may benefit from the exclusion of gain on sale of principal residence. Qualifying taxpayers may exclude up to $250,000 (or $500,000 for qualified spouses filing jointly) of gain on the sale or exchange of a principal residence. In order to qualify, you must have owned and occupied the property as your principal residence for at least two of the five previous years. A "residence" includes a house, condominium, houseboat, house trailer (mobile home), and stock held by a tenant-shareholder in a cooperative housing corporation. If you own more than one residence, your principal residence is the residence you use the majority of the time during the year.

If you are married and you file a joint return, you may exclude up to $500,000 if (1) one of you meets the ownership test, (2) both of you meet the use test, and (3) neither of you have used the benefit of the exclusion within the last two years. If you and your spouse do not meet all three requirements, the exclusion is determined on an individual basis as if you had not been married.

In certain hardship circumstances, the $250,000 ($500,000 for married couples filing jointly) exclusion is prorated if you do not meet the two-year ownership and use requirements due to a change in employment, health, or unforeseen circumstances.

Certain rules apply to taxpayers with a home office. No allocation of the exclusion is required between a home office and the remainder of your principal residence so long as the home office is located within the principal residence. However, in the event you depreciate a portion of your home for business use, you are required to recognize the amount of depreciation attributable to periods after May 6, 1997 as unrecaptured gain, and reduce the gain available for exclusion accordingly.

Keep in mind that tax planning opportunities exist for properties used as investment property. Because regulations do not require your property to be your principal residence on the sale date, provided you meet the ownership and use test, you may exclude gain on the sale as a principal residence, and if the property is investment property at the time of the exchange, defer additional gain in a like-kind exchange. Thus, with careful planning, you may benefit from both the principal residence exclusion and a like-kind deferral.

If you anticipate selling your home in the near future, these tax provisions impact you. Consequently, careful consideration of these rules should be made in order to minimize or eliminate any resulting gain from the sale of your residence. If you have any questions or would like additional explanation as to how these provisions affect you, please call our offices at your earliest convenience.