From the desk of
Peter S. Muffoletto, C.P.A.

Tax Implications when Selling your Home

Gains & Exclusion of Gain

Those who sell their home that they have claimed on their tax returns as their primary residence for at least 2 of the previous 5 years have an exceptional tax benefit in that they can exclude up to $250,000 of that gain from their income as an individual, or $500,000.00 if married.

An interesting twist to the marriage issue is that one does not necessarily need to have been married to their spouse for the entire qualifying period, but do have to file jointly for the year in which the sale is reported.

Ownership and Use

To claim the exclusion one must meet ownership and use tests.

During a five-year period ending on the date of the sale the homeowner must have owned the home and lived in it as their main home for at least two years.

Losses

Some experience a loss when their primary home sells for less than what the property cost them including improvements.

This loss is not deductible.

Multiple Homes

Those who own more than one home can only exclude the gain on the sale of their primary residence.

Many attempt to claim the exclusion for alternate properties as the one that the gain is being excluded, but there is a trap in that if the property that was sold has not been claimed as the primary residence for at least two out of the five years preceding the sale, evidenced by the address indicated on the face of their individual tax return, and further evidenced as to the property taxes, and mortgage interest claimed during the required minimum period, that attempt will under audit fail, and those claiming the exclusion will face the tax, penalties, interest, and possible fraud indictments.

Any property sold at a gain that does not qualify as the primary residence will necessarily have to pay the taxes on that gain from selling any other home, or property.

One might want to consider either an IRC 1031 Exchange, or investment in an Opportunity Zone investment to defer the taxes.

Reported Sale

Those who do not qualify to exclude all of the taxable gain from their income must report the gain from the sale of their home.

The instructions that the IRS provides states that if an exclusion under IRC 121 results in no taxable income to be reported, the sale does not need to be entered on the tax return, but we have found in practice that the IRS matching program tends to initiate inquiries if the sale including the exclusion is not reported, therefore we suggest that all sales be reported even when the exclusion results in no tax.

Mortgage Debt

In some instances when a property is sold there is debt forgiven, or canceled as part of the sale.

Forgiven or cancelled debt is taxable income.

This includes people who had a mortgage workout, foreclosure, or other canceled mortgage debt on their home.

Taxpayers who had debt discharged after December 31, 2017, cannot exclude that income as qualified principal residence indebtedness unless a written agreement for the debt forgiveness was in place before January 1, 2018.

There are some exceptions to these rules for some individuals, including persons with a disability, certain members of the military, intelligence community and Peace Corps workers.

State of California Franchise Tax Board Primary Residence Sale Audits

The State of California has discovered that many, actually most do not retain their records relating to their properties. In discovering this, the Franchise Tax Board has initiated a new audit program to audit the sale of personal residences, and if the taxpayer cannot produce records, receipts, and documentation supporting the cost and improvements of the property sold are assessing taxes, interest, and penalties for that amount that cannot be documented.

We suggest that clients retain all acquisition documentation, and fully document all improvements during the period that they hold any property.

We here at Muffoletto & Company believe that the more informed you are in regards to the rules and regulations that affect you the more we can be of service.

Should you have questions relating to any tax or financial matters call at

(818) 346-2160,

or you can visit us on the web at

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