Bottom Line Tidbits

Sale of Residence – Exclusion of Gain
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Most people are able to sell their principal residence without incurring any income tax liability. A tax provision was passed in 1997 and final regulations were issued in late 2002 providing for gain exclusion of $250,000 ($500,000 on a joint return) from the sale of a principal residence.

The basic test for qualifying for this exclusion of gain is that you must have owned and used the home as your principal residence for a period of two or more years in the five year period ending on the date you sell the residence.

The final regulations have clarified some important questions regarding this provision. For example, what kind of property can qualify as a personal residence? In addition to the traditional house, the regulations state a personal residence can include a houseboat, a house trailer, or the house or apartment the taxpayer is entitled to occupy as a tenant-stockholder in a cooperative housing corporation.

The regulations provide guidance relative to the factors to be utilized in determining a taxpayer’s principal residence. They include: 1) place of employment; 2) principal place of abode; 3) address listed on tax returns, driver’s license, voter registration; 4) mailing address for bills and correspondence; and 5) location of religious organizations and recreational clubs.

The final regulations also provides clarification permitting a fractional exclusion amount if the taxpayer fails to meet the ownership and use requirements due to a change in place of employment, health, or unforeseen circumstances. Details are available in the regulations explaining what constitutes these qualifying circumstances. The fractional exclusion is determined by the fraction of time the owned and used relative to the 2 years in the 5 years prior to the sale.

This exclusion provision is a very beneficial financial management tool for individuals desiring to sell their primary residences. There is no age requirement for the taxpayer and the funds do not have to be reinvested in another residence. For taxpayers willing to give up their large/expensive family home for a smaller/less-expensive home or home ownership altogether, this gain exclusion provision can create an attractive tax-sheltered retirement vehicle.