

**New Principal Residence Rules:**

# Treasury Decision 9030 Clarifies Section 121 Exclusions

By Kennen Cohen

Section 121 of the Internal Revenue Code allows exclusion up to \$250,000 of the capital gain on a principal residence for single taxpayers and \$500,000 for a married couple filing jointly. To qualify, the taxpayer must own and use the home as a principal residence for two of the five years prior to the sale. The ownership and use periods do not need to be concurrent. The two years may consist of 24 full months or 730 days. Treasury Decision 9030 clarifies a number of issues including exceptions to the two-year rules for use, ownership and claimed exclusion "safe harbors" when the primary reason for the sale is health, change in place of employment or "unforeseen circumstances."

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**Employment:** Exception permitted if the new job site is at least 50 miles farther from the old home than the old workplace was from that home.

**Health:** Exception permitted if the primary reason is related to a disease, illness or injury or if a physician recommends a change in residence for health reasons. In addition, a qualified person for health reasons includes close relatives, so that sales related to caring for sick family members will qualify.

**Unforeseen Circumstances:** Exceptions occurring primarily because of "unforeseen circumstances" include:

- Death;
- Divorce or legal separation;
- Becoming eligible for unemployment compensation;
- Change in employment that leaves the taxpayer unable to pay the mortgage or reasonable basic living expenses;
- Multiple births resulting from the same pregnancy;
- Damage to the residence resulting from a natural or man-made disaster;
- Act of war or terrorism; condemnation, seizure or other involuntary conversions of the property.

Any of the first five situations listed above must involve the taxpayer, spouse, co-owner or a member of the taxpayer's household to qualify. The Regulations also give the IRS Commissioner the discretion to determine other circumstances as "unforeseen."


The Regulations list several factors relevant in determining which home is the "principal residence" of taxpayers who own more than one home. Among these factors include:

- Where other family members live;
- Place of employment;
- Amount of time used;
- Address used for tax returns, driver's license,
- Car and voter registration, bills and correspondence;
- Location of the taxpayer's bank, church and recreational clubs.

Taxpayers do not need to allocate the gain between the business and residential use if the business use occurred within the same dwelling unit as the residential use. Capital gain taxes must be paid on the total depreciation taken after May 6, 1997, but may exclude additional gain on the residence, up to the maximum amount.

The principal residence exclusion may include capital gain from the sale of vacant land that has been used as part of the residence, if the land sale occurs within two years before or after the sale of the residence.

Treasury Decision 9030, the final home sale regulations, and T.D. 9031 are published in the Federal Register available at [www.federalregister.gov](http://www.federalregister.gov). Every taxpayer should review their specific transaction with their own tax and/or legal advisors. This information is not intended to replace qualified tax or legal counsel. ■



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