

While Taxpayers were inhabiting House 1, A, a family member and inhabitant of the Taxpayer's house, was placed on probation and spent one year at a rehabilitation facility. Because Taxpayers wanted to move from the neighborhood, Taxpayers sold House 1 and bought House 2 during the year that A was living in the rehabilitation facility.

Taxpayers began to use House 2 as their principal residence in Month 1, Year 2. At the time that the Taxpayers bought House 2 and starting using House 2 as their principal residence, Taxpayers expected that A would not inhabit House 2 on a permanent basis. However, in Month 2, Year 2, the court ordered A to live at House 2 under house arrest and to continue receiving rehabilitation counseling.

According to Taxpayers statements, their neighbors have vehemently protested A's presence in the neighborhood and the neighborhood hostility makes living in House 2 intolerable. Their neighbors have made threats against A, have insisted that A not spend time outside in the Taxpayer's yard, and have interfered with A's attempts to find employment. In addition, A's probation officer believes that selling Taxpayer's house and moving Taxpayer's family to another neighborhood would improve A's chances of ending or reducing the period of A's probation and house arrest.

LAW & ANALYSIS

Section 121(a) of the Code provides that a taxpayer's gross income will not include gain from the sale or exchange of property if, during the five-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating two years or more. The full exclusion is available only once every two years.

The maximum exclusion amount is \$500,000 if (1) a husband and wife file a joint return for the year of the sale, (2) both spouses meet the 2-year use test, (3) at least one of the spouses meets the 2-year ownership test, and (4) neither spouse used the section 121 exclusion during the last two years.

For taxpayers who fail to satisfy the ownership and use tests or the limit of one sale every two years, section 121(c) of the Code provides for a reduced maximum exclusion if the primary reason for sale or exchange is a change in place of employment, health, or unforeseen circumstances.

The temporary regulations provide that a sale or exchange is by reason of unforeseen circumstances if the primary reason for the sale or exchange is the occurrence of an event that the taxpayer does not anticipate before purchasing and occupying the residence. See section 1.121-3T(e) of the Income Tax Regulations.

PLR-135236-03

A taxpayer's primary reason for the sale or exchange is deemed to be unforeseen circumstances if one of the safe harbor events, such as involuntary conversion of the residence, death, or divorce, occurs during the period of the taxpayer's ownership and use of the residence as the taxpayer's principal residence. In addition, the Commissioner may designate other events or situations as unforeseen circumstances in published guidance of general applicability or in a ruling directed to a specific taxpayer.

The reduced maximum exclusion is computed by multiplying the maximum dollar limitation of \$250,000 (\$500,000 for certain joint filers) by a fraction. The numerator of the fraction is the shortest of the following periods: (1) the period of time that the taxpayer owned the property during the 5-year period ending on the date of the sale or exchange, (2) the period of time that the taxpayer used the property as the taxpayer's principal residence during the 5-year period ending on the date of the sale or exchange, or (3) the period of time between the date of a prior sale or exchange of property for which the taxpayer excluded gain under § 121 and the date of the current sale or exchange. The numerator of the fraction may be expressed in days or months. The denominator of the fraction is 730 days or 24 months (depending on the measure of time used in the numerator).

Based on the facts as represented and the relevant law as set forth above, we conclude that your primary reason for the sale of House 2 will be an unforeseen circumstance. Consequently, if you sell House 2 when you have owned and used it as your principal residence for less than two of the preceding five years, you will be entitled to exclude gain up to the reduced maximum exclusion amount under section 121(c) of the Code.

Except as specifically ruled upon above, no opinion is expressed or implied regarding the income tax consequences of any transaction, or any item discussed or referenced in this letter. In addition, no opinion is expressed or implied as to whether you have used the Residence as your principal residence.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed

PLR-135236-03

by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

William A. Jackson
Chief, Branch 5
Office of Income Tax and Accounting