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Selling Your Home

For use in preparing
1994 Returns

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Important Change for 1994

Moving expenses. If you incurred selling expenses after December 31, 1993, you no longer have the option of deducting some of the expenses as moving expenses. They are only deductible as selling expenses. See *Selling expenses* under *Old Home*.

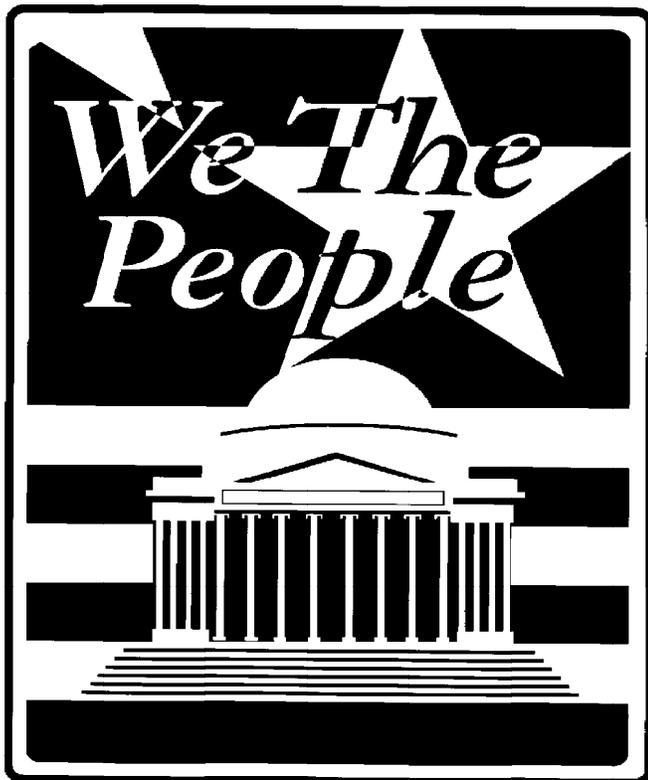
Important Reminders

Change of address. If you change your mailing address, be sure to notify the IRS using Form 8822, *Change of Address*. Mail it to the Internal Revenue Service Center for your old address (addresses for the Service Centers are on the back of the form).

Seller-financed mortgages. If you sold your home and hold a note, mortgage, or other financial agreement, you may have to report the buyer's name, address, and social security number (SSN) when you report the interest income. See *Installment sale* under *How and When to Report*, later.

Abandonment, foreclosure, or repossession. If your home was abandoned, foreclosed on, or repossessed, you have a sale or disposition that you should report on Form 2119, *Sale of Your Home*. If the disposition resulted in a taxable gain, also report it on Schedule D (Form 1040).

Generally, you will receive **Form 1099-A, Acquisition or Abandonment of Secured Property**, from the lender who acquired the property. This form will have the information you need to determine whether you have a capital gain or loss, or ordinary income. If your debt is canceled, you may also receive **Form**



1099-C, Cancellation of Debt, showing the amount of the canceled debt. See *Foreclosures and Repossessions* in Chapter 1 and *Abandonments* in Chapter 2 of Publication 544, *Sales and Other Dispositions of Assets*, for more information.

Combat zone service. The replacement period for postponing tax on any gain from the sale of your home is suspended if you served in the Persian Gulf Area combat zone. For this suspension, the area is considered a combat zone beginning August 2, 1990. See *Time Allowed for Replacement under Postponement of Gain*, later, for more information.

Form 1099-S. The law requires that transactions involving the sale of most residential real estate property be reported to the IRS on Form 1099-S, *Proceeds From Real Estate Transactions*. Real estate brokers are prohibited from charging any customer separately for preparing Form 1099-S.

Maximum tax rate on capital gains. A taxable gain on the sale of your home is a capital gain. The maximum tax rate on a net capital gain is 28%. See *How and When to Report*, later.

Qualified mortgage bonds and mortgage credit certificates. If you sell your main home that was purchased or improved with federally subsidized financing, you may have to recapture part of the subsidy. See *Recapture of Federal Subsidy*, later.

Home sold with undeducted points. If you have not deducted all the points you paid to secure a mortgage on your old home, you may be able to deduct the remaining points in the year of sale. See *Points* in Part I of Publication 936, *Home Mortgage Interest Deduction*.

Introduction

If you have a gain from the sale of your main home (generally, the one in which you live), the gain may be:

- Postponed,
- Excluded (once-in-a-lifetime),
- Included on your return, or
- Treated as a combination of the above.

If you have a loss from the sale of your main home, it is a personal loss. You must report the sale on your return, but you cannot deduct the loss.

This publication explains how to treat any gain or loss from selling your main home. It covers how to postpone paying tax on all or part of the gain, how to make the one-time election to exclude gain, and how to report the sale on your return.

You must report the sale of your main home using Form 2119, *Sale of Your Home*. This is true whether you sell the home at a gain or a loss and whether or not you buy another main home.

How you treat the gain on the sale of your main home depends on several factors, such as:

- The amount of your gain,
- Your plans to replace the home,
- Whether you were age 55 or older on the date of sale,
- How long you owned and lived in the home, and
- Whether you sold any other home(s) previously.

If you exchange your home for other property, the exchange is treated as the sale of your home. In this publication, “sale” also means “exchange,” and the same rules apply. However, if you transfer your home to your spouse, or former spouse incident to your divorce, no gain or loss is recognized on the transfer. Therefore, the rules explained in this publication do not apply. See *Property Settlements* in Publication 504, *Divorced or Separated Individuals*, for more information.

This publication does not cover the sale of your second home or your vacation home. For information on how to report those sales, see Publication 544, *Sales and Other Dispositions of Assets*. It also does not cover the sale of rental property. For information on selling your rental property, see Publication 527, *Residential Rental Property*.

Definitions. Many of the terms used in this publication, such as “adjusted sales price,” “postponement of gain,” and “one-time exclusion” are defined in the *Glossary* at the end of this publication.

Useful Items

You may want to see:

Publication

- 521** Moving Expenses
- 527** Residential Rental Property
- 530** Tax Information for First-Time Homeowners
- 544** Sales and Other Dispositions of Assets
- 551** Basis of Assets
- 587** Business Use of Your Home
- 936** Home Mortgage Interest Deduction

Form (and Instructions)

- Schedule D (Form 1040)** Capital Gains and Losses
- 1040X** Amended U.S. Individual Income Tax Return
- 2119** Sale of Your Home
- 8822** Change of Address
- 8828** Recapture of Federal Mortgage Subsidy

Ordering publications and forms. To order free publications and forms, call our toll-free

telephone number 1-800-TAX-FORM (1-800-829-3676). If you have access to TDD equipment, you can call 1-800-829-4059. See your tax package for the hours of operation. You can also write to the IRS Forms Distribution Center nearest you. Check your income tax package for the address.

Asking tax questions. You can call the IRS with your tax question Monday through Friday during regular business hours. Check your telephone book or your tax package for the local number or you can call toll-free 1-800-829-1040 (1-800-829-4059 for TDD users).

Gain or Loss On the Sale

Words you may need to know (see Glossary):

Adjusted sales price
Gain
Postponement of gain

If you sell your main home, you may have to postpone paying tax on all or part of the gain from the sale. If you have a loss on the sale, you cannot deduct it.

Gain on sale. You *must postpone* the tax on all the gain from the sale if you buy a new home and the purchase price of the new home is at least as much as the adjusted sales price of the old home.

You will generally be subject to tax on all or part of the gain if you do not buy a new home, or if the purchase price of the new home is less than the adjusted sales price of the old home. However, if you are age 55 or older, you may qualify to exclude the gain as explained later.

Loss on sale. You *cannot* deduct a loss on the sale of your home. It is a personal loss. However, you must report the sale on Form 2119. The loss has no effect on the basis of your new home.

Joint ownership. If you and your spouse sell your jointly owned home and file a joint return, you figure and report your gain or loss as one taxpayer. If you file separate returns, each of you must figure and report your own gain or loss according to your ownership interest in the home. Your ownership interest is determined by state law.

If you and a joint owner other than your spouse sell your jointly owned home, each of you must figure and report your own gain or loss according to your ownership interest in the home. Each of you applies the rules discussed in this publication on an individual basis.

Purchase price at least as much as sales price. Your entire gain on the sale of your home is not taxed at the time of the sale if,

within **2 years before or 2 years after** the sale, you buy and live in another home that costs at least as much as the adjusted sales price (described later) of the old home. If you are on active duty in the Armed Forces, if you served in a combat zone, or if your tax home is outside the U.S., the 2-year period after the sale may be suspended. See *People Outside the U.S. and Members of the Armed Forces under Time Allowed for Replacement*, later.

Purchase price less than sales price. If the purchase price of your new home is less than the adjusted sales price of your old home and you buy and live in the new home within 2 years before or 2 years after the sale, the gain taxed in the year of the sale is the lesser of:

- 1) The gain on the sale of the old home (reduced by any gain you exclude as explained later under *Exclusion of Gain*, or
- 2) The amount by which the adjusted sales price of the old home is more than the purchase price of the new home.

You need not use the same funds received from the sale of your old home to buy or build your new home. For example, you can use less cash than you received by increasing the amount of your mortgage loan and still postpone the tax on your gain.

Reimbursement from your employer. You must include in income any amount your employer reimburses you for a loss on the sale of your home or for expenses of the sale when you transfer to a new location. Do **not** include the payment as part of the selling price. Include it in your gross income as compensation for services on line 7 of Form 1040. For more information, see *How to Report* in Publication 521.

You may owe estimated tax. If you have a taxable gain from the sale of your home and you do not plan to replace it, or if you do not meet the requirements for postponing tax on the gain, you may have to make estimated tax payments. For more information, see Publication 505, *Tax Withholding and Estimated Tax*.

Recapture of Federal Subsidy

If you financed your home under a federally subsidized program (loans from tax-exempt qualified mortgage bonds or loans with mortgage credit certificates), you may have to recapture all or part of the benefit you received from that program when you sell or otherwise dispose of your home. You recapture the benefit by increasing your federal income tax for the year of the sale. The postponement and exclusion of gain provisions discussed later in this publication do not apply to this recapture tax.

The recapture tax is figured on **Form 8828**. If your mortgage loan is subject to the recapture rules, you must file Form 8828 even if you

do not owe a recapture tax. See *How to report the recapture*, later.

Loans subject to recapture rules. The recapture of the subsidy applies to loans provided after 1990 that:

- 1) Came from the proceeds of qualified mortgage bonds issued after August 15, 1986, or
- 2) Were based on mortgage credit certificates issued after December 31, 1990.

The recapture also applies to assumptions of these loans.

If your mortgage loan is subject to the recapture rules, you should have received a notice containing information that you need to figure the recapture tax. See *Notice of amounts*, later.

Federal subsidy benefit. If you received a mortgage loan from the proceeds of a tax-exempt bond, you received the benefit of a lower interest rate than was customarily charged on other mortgage loans. If you received a mortgage credit certificate with your mortgage loan, you were able to reduce your federal income taxes by a mortgage interest tax credit.

When the recapture applies. The recapture of the federal mortgage subsidy applies only if you meet **all** of the following conditions.

- 1) You sell or otherwise dispose of your home at a gain,
- 2) Your income for the year of disposition exceeds that year's adjusted qualifying income for your family size for that year (related to the income requirements a person must meet to qualify for the federally subsidized program), and
- 3) You dispose of your home during the first 9 years after the date you closed your mortgage loan.

When recapture does not apply. The recapture does **not** apply if any of the following situations apply to you:

- The mortgage was secured solely as a qualified home improvement loan not in excess of \$15,000,
- The home is disposed of as a result of your death,
- You dispose of the home more than 9 years after the date you closed your mortgage loan,
- You transfer the home to your spouse, or to your former spouse incident to a divorce, where no gain is included in your income,
- You dispose of the home at a loss,
- Your home is destroyed by a casualty, and you repair it or replace it on its original site within 2 years after the destruction, or
- You refinance your mortgage loan and the loan was based on a mortgage credit certificate (unless you later meet all of the conditions listed previously under *When the recapture applies*).

Sale or other disposition. The sale or other disposition of your home includes disposition by sale, exchange, involuntary conversion, or any other disposition.

For example, if you **give away** your home, you are considered to have "sold" it.

If you dispose of your home other than by sale, exchange, or involuntary conversion, you figure your recapture tax as if you had sold your home for its fair market value on the date you gave it away.

Notice of amounts. At or near the time of settlement of your mortgage loan, you should receive a notice that provides the federally subsidized amount and, for each year of the 9-year recapture period:

- The holding period percentage,
- The adjusted qualifying income for a family of less than three, and
- The adjusted qualifying income for a family of three or more.

You will need these amounts to figure your recapture tax, as explained next.

How to figure the recapture. The actual amount of tax you must recapture is the lesser of:

- 1) 50% of your gain on the disposition of your home, regardless of whether you have to include that gain in your income for federal income tax purposes, or
- 2) Your recapture amount.

Gain. Your gain on the disposition is the amount realized minus the adjusted basis of your home. However, in figuring your adjusted basis solely for purposes of this recapture rule, you do not subtract any postponed gain from the sale or involuntary conversion of a previous home. For more information on your adjusted basis, see *Adjusted Basis* under *Basis*, later.

Recapture amount. You determine your recapture amount by multiplying the following three items:

- 1) Your federally subsidized amount,
- 2) Your holding period percentage (based on the number of years you owned the home), and
- 3) Your income percentage.

The first two items will be found in the notice you received at or near the time of settlement of your mortgage loan. See *Notice of amounts*, earlier. Use the following steps to determine your income percentage.

Step 1. Figure your modified adjusted gross income (modified AGI) for the year of disposition. This is your adjusted gross income (AGI):

- Increased by any tax-exempt interest income for the year, and
- Decreased by any gain from the disposition of your home that is included in your gross income for the year.

Step 2. If the adjusted qualifying income amount for your family size for the year of disposition (see *Notice of amounts*, earlier) is equal to or more than your modified AGI, stop here. Your income percentage is zero and you owe no recapture tax. Otherwise, subtract the adjusted qualifying income amount from your modified AGI.

Step 3. If the amount you figured in Step 2 is \$5,000 or more, your income percentage is 100%. Otherwise, divide the amount you figured in Step 2 by \$5,000. The result is your income percentage.

How to report the recapture. If your mortgage loan is subject to the recapture rule, you will need to fill out **Form 8828**. Attach it to your Form 1040. You must file Form 8828 even if you do not owe a recapture tax. See the instructions for Form 8828 for information on how to complete the form.

Postponement of Gain

Words you may need to know (see Glossary):

- Adjusted basis
- Adjusted sales price
- Amount realized
- Basis
- Date of sale
- Fixing-up expenses
- Gain
- Improvements
- Main home
- Postponement of gain
- Repairs
- Replacement period
- Seller-financed mortgage
- Selling expenses
- Settlement fees (or closing costs)

Generally, you **must** postpone tax on the gain on the sale of your main home if you buy a new main home within the replacement period and it costs at least as much as the adjusted sales price of the old home. However, if you are age 55 or older and meet certain qualifications, no tax applies to the extent you elect to exclude the gain. See *Exclusion of Gain*, later.

This section of the publication explains the time allowed for replacement, how to determine the taxable gain, if any, and how to report the sale.

The tax on the gain is **postponed, not forgiven**. You subtract any gain that is not taxed in the year you sell your old home from the cost of your new home. This gives you a lower basis in the new home. If you sell the new home in a later year and again replace it, you continue to postpone tax on your gain.

Example. You sold your home in 1994 for \$90,000 and had a \$5,000 gain. Within the time allowed for replacement, you bought another home for \$103,000. The \$5,000 gain will

not be taxed in 1994 (the year of sale), but you must subtract it from the \$103,000. This makes the basis of your new home \$98,000. If you later sell the new home for \$110,000, and you do not buy and live in a replacement home within the allowed time, you will be subject to tax on the \$12,000 gain (\$110,000 – \$98,000) in the year of that sale.

Main Home

Usually, the home in which you live is your main home. The home you sell and the one you buy to replace it must both qualify as your main home. *Property used partly as your home and partly for business or rental*, and *Home changed to rental property*, are discussed later under *Old Home*.

Your main home can be a houseboat, a mobile home, a cooperative apartment, or a condominium.

Fixtures (permanent parts of the property) generally are part of your main home. Furniture, appliances, and similar items that are not fixtures generally are not part of your main home.

Land. You may sell the land on which your main home is located, but not the house itself. In this case, you cannot postpone tax on any gain you have from the sale of the land.

Example. You sell the land on which your main home is located. Within the replacement period, you buy another piece of land and move your house to it. This sale is not considered a sale of your main home, and you cannot postpone tax on any gain on the sale.

More than one home. If you have more than one home, only the sale of your main home qualifies for postponing the tax. If you have two homes and live in both of them, your main home is the one you live in most of the time.

Example 1. You own and live in a house in town. You also own beach property, which you use in the summer months. The town property is your main home; the beach property is not.

Example 2. You own a house, but you live in another house that you rent. The rented home is your main home.

However, if a house you own is your main home, you can temporarily rent it out before its sale without changing its character as your main home.

Time Allowed for Replacement

You must buy or build and live in another house within **2 years before or 2 years after** the date of sale of your old home to postpone the tax on the gain from the sale.

Example. On April 27, 1994, before you sell your old home, you buy and move into a new home that you use as your main home. You have until April 27, 1996, a period of 2 years, to sell your old home and postpone tax on any gain.

Occupancy test. You must physically live in the replacement home as your main home

within the required period. If you move furniture or other personal belongings into the new home but do not actually live in it, you have not met the occupancy test.

No added time beyond the specified period is allowed. To postpone gain on the sale of your home, you must replace the old home and occupy the new home within the specified period. You are not allowed any additional time, even if conditions beyond your control keep you from doing it. For example, destruction of the new home while it was being built would not extend the replacement period. However, there may be a suspension of the replacement period, discussed later, for people outside the U.S. or members of the Armed Forces.

If you do not replace the home in time and you had postponed gain in the year of sale, you must file an amended return for the year of sale. You must include in your income the entire gain on the sale of your old home. Also, if you began building your new home within the specified period, but for any reason were unable to live in it within 2 years, no more time for occupancy is allowed. You must report your entire gain on an amended return for the year of sale. See *Amended Return*, later.

People Outside the U.S.

The replacement period after the sale of your old home is suspended while you have your **tax home** (the place where you live and work) outside the U.S. This suspension applies only if your stay abroad begins before the end of the 2-year replacement period. The replacement period, plus the period of suspension, is limited to **4 years** after the date of sale of your old home.

Example. You sold your home on May 11, 1994. This began your replacement period. On September 11, 1994, you were transferred to a foreign country. You have used 4 months of your replacement period. From September 11, 1994, to June 10, 1996, when you return to the U.S., your replacement period is suspended. Your replacement period starts again on June 11, 1996, and ends on February 11, 1998 (20 months).

Married persons. If you are married, the suspension of the replacement period lasts while either you or your spouse has a tax home outside the U.S., provided both of you used the old and the new homes as your main home.

Tax home. Your tax home is the city or general area of your main place of business, employment, station, or post of duty. For your tax home to be outside the U.S., you must live and work there. However, it does not matter where your family lives. More information on a tax home outside the U.S. is in Publication 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad*.

Nonmilitary service in a combat zone in support of the Armed Forces. The running of the replacement period (including the suspension if you live and work outside the U.S.) is suspended for any period you served in the Persian Gulf Area combat zone in support of

the Armed Forces, plus 180 days, even though you were not a member of those forces. This includes Red Cross personnel, accredited correspondents, and civilians under the direction of the Armed Forces in support of those forces.

The rules for suspending the running of the replacement period and for applying that suspension to your spouse are the same as the suspension rules explained later under *Members of the Armed Forces* and its discussion, *Military service in a combat zone*.

Members of the Armed Forces

The replacement period after the sale of your old home is suspended while you serve on extended active duty in the Armed Forces. You are on extended active duty if you are serving under a call or order for more than 90 days or for an indefinite period. The suspension applies only if your service begins before the end of the 2-year replacement period. The replacement period, plus any period of suspension, is limited to **4 years** after the date you sold your old home.

Example 1. You sold your home on May 1, 1992. This began your replacement period. You joined the Armed Forces on August 1, 1992. You have used 3 months of your replacement period (May, June, and July). Your active duty ends July 31, 1994. From August 1, 1992, to July 31, 1994, your replacement period is suspended. Your replacement period starts again on August 1, 1994, and you have until May 1, 1996 (21 months) to buy and live in your new home.

Example 2. You are a regular member of the Armed Forces and sold your home on June 5, 1993. If you remain in the Armed Forces, you can postpone your gain from the sale of your old home only if you buy or build and live in another home by June 5, 1997.

Overseas military assignment. The suspension of the replacement period after the sale of your old home is extended for up to an additional 4 years while you are stationed outside the U.S. This also applies while you are required to live in on-base quarters following your return from a tour of duty outside the U.S. In this case, you must be stationed at a remote site where the Secretary of Defense has determined that adequate off-base housing is not available.

The suspension can continue for up to 1 year after the last day you are stationed outside the U.S. or the last day you are required to reside in government quarters on base. However, the replacement period, plus any period of suspension, is limited to **8 years** after the date of sale of your old home.

If you qualify for the time suspension for members of the Armed Forces and have already filed an income tax return reporting gain from the sale of a home that can be further postponed, you can file Form 1040X to claim a refund. See *Amended Return*, later, for the time allowed for filing an amended return.

Example 1. You are a regular member of the Armed Forces and sold your home on May 1, 1991. During the 4 years from May 1, 1991, to May 1, 1995, you serve outside the U.S.

When you return, you are stationed at a remote site and are required to live on base because off-base housing is not available. The time to replace your home is suspended:

- 1) While you are serving outside the U.S.,
- 2) While you are required to reside on base after your return from the overseas assignment, plus
- 3) Up to 1 year.

If the requirement that you live on base ends on October 31, 1995, the suspension period expires October 31, 1996. You then have the full 2-year replacement period to buy or build and occupy a new home. This is because you did not use any of that time before your overseas assignment began, and your replacement period plus your 5½ year period of suspension will not end before the 8-year limit after the sale of your old home. Your replacement period ends on October 31, 1998.

Example 2. Assume the same facts as in Example 1 except the requirement that you live on base ends on October 31, 1996. The suspension period expires October 31, 1997. You then have less than the full 2-year replacement period to buy or build and occupy a new home. This is because your replacement period plus your 6½ year period of suspension is limited to 8 years after the sale of your old home. Therefore, your replacement period ends on April 30, 1999.

Spouse in Armed Forces. If your spouse is in the Armed Forces and you are not, the suspension also applies to you if you owned the old home. Both of you must have used the old home and must use the new home as your main home. However, if you are divorced or separated while the replacement period is suspended, the suspension ends for you on the date of the divorce or separation.

Military service in a combat zone. The running of the replacement period (including any suspension) is suspended for any period you served in the Persian Gulf Area combat zone. For this suspension, the designation of the area as a combat zone is effective August 2, 1990.

If you performed military service in an area outside the combat zone that was in direct support of military operations in the combat zone **and** you received special pay for duty subject to hostile fire or imminent danger, you are treated as if you served in the combat zone.

This suspension ends 180 days after the later of:

- 1) The last day you were in the combat zone (or, if earlier, the last day the area qualified as a combat zone), or
- 2) The last day of any continuous hospitalization (limited to 5 years if hospitalized in the U.S.) for an injury sustained while serving in the combat zone.

For information on other tax benefits available to those who served in a combat zone,

Figure A. An Illustration of the Time Allowed for Replacement

This illustrates the time period during which you can replace your main home and postpone tax on the gain from its sale. It does not apply if you served in the Persian Gulf Area combat zone. Caution: The dates in this chart are for illustration purposes only. Your dates may be different.		
	If you sold your former home on June 30, 1994:	
	Your time for replacement begins on:	Your time for replacement ends on or before:
Most taxpayers	June 30, 1992 (2 years before sale)	June 30, 1996 (2 years after sale)
Certain people outside the U.S. and members of the Armed Forces ¹	June 30, 1992 (2 years before sale)	June 30, 1998 (4 years after sale)
Certain members of the Armed Forces stationed overseas ²	June 30, 1992 (2 years before sale)	June 30, 2002 (8 years after sale)

¹ Your 2-year replacement period after the sale can be suspended while you live and work outside the U.S. or are on extended active duty in the Armed Forces. However, your replacement period, plus any period of suspension, cannot exceed 4 years after the date of sale of your old home. See *People Outside the U.S. or Members of the Armed Forces*.

² Your 2-year replacement period after the sale can be suspended while you are stationed outside the U.S. or required to live in on-base quarters after returning from a tour of duty outside the U.S. However, your replacement period, plus any period of suspension, cannot exceed 8 years after the date of sale of your old home. See *Overseas military assignment* under *Members of the Armed Forces*.

get Publication 945, *Tax Information for Those Affected by Operation Desert Storm*.

Example. Sergeant James Smith, on extended active duty in an Army unit stationed in Virginia, had a gain from the sale of his home on June 4, 1990. He had not yet purchased a replacement home when he entered the Persian Gulf Area combat zone on September 4, 1990. He left the combat zone on May 4, 1991, and returned with his unit to Virginia. He remains on active duty in Virginia.

Sergeant Smith's replacement period began on June 4, 1990, the date he sold the home. His replacement period would have ended 4 years later, on June 4, 1994.

When he entered the combat zone on September 4, 1990, Sergeant Smith had used 3 months of the replacement period. The replacement period was then suspended for the time he served in the combat zone plus 180 days. The replacement period started again on November 1, 1991, after the end of the 180-day period (May 5, 1991, to October 31, 1991) following his last day in the combat zone. Sergeant Smith then has 45 months remaining in his replacement period (4 years minus the 3 months already used). His replacement period will end July 31, 1995 (45 months after October 31, 1991).

Spouse. This suspension generally applies to your spouse (even if you file separate returns). However, any suspension for hospitalization within the U.S. does not apply to your spouse. Also, the suspension for your spouse does not apply for any tax year beginning more than 2 years after the last day the area qualified as a combat zone.

Amended Return

If you sell your old home and do not plan to replace it, you must include the gain in income for the year of sale. If you later change your mind, buy or build and live in another home within the replacement period, and meet the requirements to postpone gain, you will have to file an amended return (Form 1040X) for the year of sale to claim a refund.

You can file an amended return by the later of:

- 1) 3 years from the date you filed the return, or
- 2) 2 years from the date you paid the tax.

A return filed before the due date is treated as filed on the due date.

Extended replacement period. If you have an extended replacement period because you have your tax home outside the U.S. or are a member of the Armed Forces, the replacement period may go beyond the last date you can file an amended return claiming a refund for the year of sale. If there is a possibility you may change your mind and buy another home during the extended replacement period, you should file a *protective claim* for refund of the tax you paid on the gain. File this claim on Form 1040X at the same time you file the return for the year of sale or anytime within the period allowed for filing an amended return.

Protective claim. To file a protective claim for refund, use Form 1040X and its instructions. However, you may leave lines 1 through 23 blank on the front of the form if you do not know the amount of your postponed gain at the time you file it. In *Part II* of the form:

- 1) Write "Protective Claim,"
- 2) Explain that you paid tax on the gain from the sale of your old home,
- 3) State the amount of the gain you reported on your original return,
- 4) State that you have an extended replacement period and why this extended period applies to your particular situation, and
- 5) State that you are filing this protective claim because during your extended replacement period you may buy (or build) a new main home.

Basis

You will need to know your basis in your home as a starting point for determining any gain or loss when you sell it. Your basis in your home is determined by how you acquired it. Your basis is its cost if you bought it or built it. If you acquired it in some other way, its basis is either its fair market value when you received it or the adjusted basis of the person you received it from.

While you owned your home, you may have made adjustments (increases or decreases) to the basis. This adjusted basis is used to figure gain or loss on the sale of your home.

Cost As Basis

The cost of property is the amount you pay for it in cash or other property.

Purchase. The basis of your home is the cost of the property to you. This includes the purchase price and certain settlement or closing costs. Your basis includes your down payment and any debt, such as a first or second mortgage or notes you gave the seller in payment for the property. You may have to reduce the basis by points the seller paid for you. For more information, see *Seller-paid points*, next, and *Settlement fees or closing costs*, under *New Home*, later.

Seller-paid points. If you bought your home after April 3, 1994, you must reduce the basis of your home by any points the seller paid. If you bought your home after 1990 but before April 4, 1994, and you chose to deduct the seller-paid points, you must reduce your basis by the amount of these points.

Construction. If you contracted to have your house built on land you own, your basis is the cost of the land plus the amount it cost you to complete the house. This includes the cost of labor and materials, or the amounts paid to the contractor, and any architect's fees, building permit charges, utility meter and connection charges, and legal fees directly connected with building your home. Your basis includes your down payment and any debt, such as a first or second mortgage or notes you gave the

seller or builder. It also includes certain settlement or closing costs. You may have to reduce the basis by points the seller paid for you. For more information, see *Seller-paid points*, earlier, and *Settlement fees or closing costs*, under *New Home*, later.

If you built all or part of your house yourself, its basis is the total amount it cost you to complete it. Do not include the value of your own labor, or any other labor you did not pay for, in the cost of the house.

Cooperative apartment. Your basis in the apartment is usually the cost of your stock in the co-op housing corporation, which may include your share of a mortgage on the apartment building.

Condominium. Your basis is generally its cost to you.

Other Basis

Sometimes you must use a basis other than cost, such as fair market value. For a complete discussion of basis, see Publication 551.

Fair market value. Fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither having to buy or sell, and both having reasonable knowledge of the relevant facts. Sales of similar property, on or about the same date, may be helpful in figuring the fair market value of the property.

Gift. If your home was a gift, its basis to you is the same as the donor's adjusted basis when the gift was made. However, if the donor's adjusted basis was more than the fair market value of the home when it was given to you, you must use that fair market value as your basis for measuring any loss on its sale.

If you use the donor's adjusted basis to measure a gain and get a loss, then use the fair market value for figuring a loss and get a gain, you have neither a gain nor a loss on its sale or disposition.

Federal gift tax. If you received your home as a gift *before 1977* and its fair market value was more than the donor's adjusted basis at the time of the gift, add to your basis any federal gift tax paid on the gift. However, do not increase the basis above the fair market value of the home when it was given to you.

If you received your home as a gift *after 1976*, add to your basis the part of the federal gift tax paid that is due to the net increase in value of the home. Figure this part by multiplying the total federal gift tax paid by a fraction. The numerator (top part) of the fraction is the net increase in value of the home and the denominator (bottom part) is the fair market value of the home. The net increase in value of the home is its fair market value minus the donor's adjusted basis.

Home received from spouse. You may have received your home from your spouse or former spouse incident to your divorce. If you received the home after July 18, 1984, no gain or loss was recognized on the transfer. Your basis in this home is generally the same as your

spouse's (or former spouse's) adjusted basis just before you received it. This rule applies even if you received the home in exchange for cash, the release of marital rights, the assumption of liabilities, or other consideration.

If you received your home before July 19, 1984, in exchange for your release of marital rights, your basis in the home is generally its fair market value at the time you received it.

For more information on property acquired from a spouse or former spouse, see *Property Settlements* in Publication 504, *Divorced or Separated Individuals*.

Inheritance. If you inherited your home, the basis of the home is its fair market value on the date of the decedent's death or the later alternate valuation date if that date was used for federal estate tax purposes. If an estate tax return was filed, the value listed there for the property generally is your basis. If a federal estate tax return did not have to be filed, your basis in the home is its appraised value at the date of death for state inheritance or transmission taxes.

If you are a surviving spouse and you owned your home jointly, your basis in the home will change. The new basis for the half interest owned by your spouse will be one-half of the fair market value on the date of death (or alternate valuation date). The basis in your half will remain one-half of the adjusted basis determined previously. Your new basis is the total of these two amounts.

Example. Your jointly owned home had an adjusted basis of \$50,000 on the date of your spouse's death, and the fair market value on that date was \$100,000. Your new basis in the home is \$75,000 (\$25,000 for one-half the adjusted basis plus \$50,000 for one-half the fair market value).

Community property. In community property states (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin), the husband and wife are each usually considered to own half the community property. When either spouse dies, the fair market value of the community property at the date of death, or the alternate valuation date if chosen, generally becomes the basis of the entire property, even the portion belonging to the surviving spouse. For this to apply, at least half the community interest must be includible in the decedent's gross estate, whether or not the estate must file a return.

For more information about community property, see Publication 555, *Federal Tax Information on Community Property*.

Home received in trade. If you acquired your home in a trade for other property, the basis of your home is generally its fair market value at the time of the trade. If you traded your old home for your present home and realized a gain, see *Trading homes*, later.

Adjusted Basis

Adjusted basis is your basis **increased** or **decreased** by certain amounts.

Increases to basis. This includes any:

- 1) Improvements.
- 2) Additions.
- 3) Special assessments for local improvements.
- 4) Amounts spent after a casualty to restore damaged property.

Decreases to basis. This includes any:

- 1) Gain from the sale of your old home on which tax was postponed.
- 2) Insurance reimbursements for casualty losses.
- 3) Deductible casualty losses not covered by insurance.
- 4) Payments received for easement or right-of-way granted.
- 5) Depreciation allowed or allowable if you used your home for business or rental purposes.
- 6) Residential energy credit (generally allowed from 1977 through 1987) claimed for the cost of energy improvements that you added to the basis of your home.
- 7) Energy conservation subsidy excluded from your gross income because you received it (directly or indirectly) from a public utility after December 31, 1992, for the purchase or installation of any energy conservation measure.

Energy conservation measure. This includes installations or modifications that are primarily designed to reduce consumption of electricity or natural gas, or improve the management of energy demand for a home.

No effect on basis. Items that you cannot deduct from, or add to, your basis include:

- 1) Certain settlement fees or closing costs. These include:
 - Fire insurance premiums.
 - Mortgage insurance premiums (including VA funding fees).
 - Rent for occupancy of the house before closing.
 - Charges for utilities or other services relating to occupancy of the house before closing.
- 2) The cost of repairs.
- 3) Any item that you deducted as a moving expense.

Improvements. These are costs that add to the value of your home, prolong its useful life, or adapt it to new uses. You add the cost of improvements to the basis of your property.

Examples. Putting a recreation room in your unfinished basement, adding another bathroom or bedroom, putting up a fence, putting in new plumbing or wiring, putting on a

new roof, or paving your driveway are improvements you add to basis.

For a list of some other examples of improvements, see *Table 1*.

Repairs. These are costs that maintain your home in good condition. They do not add to its value or prolong its life, and you do not add them to the basis of your property.

Examples. Repainting your house inside or outside, fixing your gutters or floors, repairing leaks or plastering, and replacing broken window panes are examples of repairs.

Exception. The entire job is considered an improvement, however, if items that would otherwise be considered repairs are done as part of extensive remodeling or restoration of your home.

Recordkeeping. You should keep records of your home's purchase price and purchase expenses. You should also save receipts and other records for all improvements, additions, and other items that affect the basis of your home. This includes any Form 2119 that you filed to report postponement of gain from the sale of a previous home.

Ordinarily, you must keep records for 3 years after the due date for filing your return for the tax year in which you sold, or otherwise disposed of, your home. But if you use the basis of your old home in figuring the basis of your new one, such as when you sell your old home and postpone tax on any gain, you should keep those records longer. Keep those records as long as they are needed for tax purposes.

Old Home

Gain or loss on the sale of your old home is figured in Part I of Form 2119. To figure the gain or loss, you must know the selling price, the amount realized, and the adjusted basis.

You use Part III of Form 2119 to figure the adjusted sales price, the taxable gain, and the postponed gain.

Selling price. The selling price (line 4 of Form 2119) is the total amount you receive for your home. It includes money, all notes, mortgages, or other debts assumed by the buyer as part of the sale, and the fair market value of any other property you receive.

If you received a Form 1099-S, *Proceeds From Real Estate Transactions*, the total amount you received for your home (except for the fair market value of any other property or services you received or will receive) should be shown in box 2. If you received or will receive any other property or services as part of the sale, the value of these items is not shown on Form 1099-S. However, box 4 of that form should be checked.

Employer reimbursement. You may have to sell your home because of a job transfer. If your employer pays you for a loss on the sale or for your selling expenses, do **not** include the payment (reimbursement) as part of the selling price. Include it in your gross income as wages on line 7 of Form 1040. For

Table 1. Examples of Improvements

Caution: Amounts you spend on your home that do not add much to either the value or the life of the property, but rather keep the property in good condition are considered repairs, not improvements.

<p>Additions Bedroom Bathroom Deck Garage Porch Patio</p> <p>Lawn & Grounds Landscaping Driveway Walkway Fence Retaining wall Sprinkler system Swimming pool</p> <p>Miscellaneous Storm windows, doors New roof Central vacuum Wiring upgrades Satellite dish Security system</p>	<p>Heating & Air Conditioning Heating system Central air conditioning Furnace Duct work Central humidifier Filtration system</p> <p>Plumbing Septic system Water heater Soft water system Filtration system</p> <p>Interior Improvements Built-in appliances Kitchen modernization Flooring Wall-to-wall carpeting</p> <p>Insulation Attic Walls, floor Pipes, duct work</p>
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more information, see *How to Report* in Publication 521.

Option to buy. If you grant an option to buy your home and the option is exercised, add the amount you receive for the option to the sales price of your home. If the option is not exercised, you must report the amount as ordinary income in the year the option expires. Report this amount on line 21 of Form 1040.

Selling expenses. Selling expenses (line 5 of Form 2119) include commissions, advertising, and legal fees. Loan charges paid by the seller, such as loan placement fees or "points," are usually a selling expense.

Moving expenses. If you incurred selling expenses after December 31, 1993, you no longer have the option of deducting some of these expenses as moving expenses. They are only deductible as selling expenses. See Publication 521 for information on moving expenses.

Amount realized. The amount realized (line 6 of Form 2119) is the selling price minus selling expenses.

Gain. Your gain on the sale (line 8 of Form 2119) is the amount realized minus the adjusted basis of the home (line 7 of Form 2119). See *Adjusted Basis*, discussed earlier, to figure the adjusted basis of your property. Also, the *Instructions for Form 2119* has a worksheet to help you figure the adjusted basis of your old home.

Fixing-up expenses. Fixing-up expenses (line 16 of Form 2119) are decorating and repair costs that you paid to sell the old home. For example, the costs of painting the home,

planting flowers, and replacing broken windows are fixing-up expenses. These expenses must:

- 1) Be for work done during the 90-day period ending on the day you sign the contract of sale with the buyer.
- 2) Be paid no later than 30 days after the date of sale.
- 3) Not be deductible in arriving at your taxable income.
- 4) Not be used in figuring the amount realized.
- 5) Not be capital expenditures or improvements.

Note. You deduct fixing-up expenses from the amount realized **only** in figuring the part of the gain that you postpone. You **cannot** deduct them in figuring the actual gain on the sale of the old home. If the amount realized does not exceed the cost of your new home, you postpone your entire gain. In this case, you do not need to figure your fixing-up expenses.

Adjusted sales price. Use the adjusted sales price of your old home (line 18 of Form 2119) to figure the part of your gain that you can postpone. The adjusted sales price is the amount realized minus any exclusion you claim (line 14 of Form 2119) and minus any fixing-up expenses you might have. Compare the adjusted sales price with the cost of your new home to find the amount of gain that you can postpone.

Example. Your old home had a basis of \$55,000. You signed a contract to sell it on December 17, 1993. On January 7, 1994, you sold it for \$71,400. Selling expenses were

\$5,000. During the 90-day period ending December 17, 1993, you had the following work done. You paid for the work on February 4, 1994—within 30 days after the date of sale.

Inside and outside painting	\$800
New venetian blinds and new water heater	\$900

Within the required time, you bought and lived in a new home that cost \$64,600. The gain postponed and not postponed, and the basis of your new home, are figured as follows:

<u>Gain Realized</u>	
a) Selling price of old home ...	\$71,400
b) Minus: Selling expenses ...	<u>5,000</u>
c) Amount realized on sale ...	\$66,400
d) Basis of old home	\$55,000
e) Add: Improvements (blinds and heater)	<u>900</u>
f) Adjusted basis of old home	<u>55,900</u>
g) Gain realized [(c) minus (f)]	<u>\$10,500</u>

<u>Gain Taxed in 1994</u>	
h) Amount realized on sale ...	\$66,400
i) Minus: Fixing-up expenses (painting)	<u>800</u>
j) Adjusted sales price	\$65,600
k) Minus: Cost of new home	<u>64,600</u>
l) Excess of adjusted sales price over cost of new home	<u>\$ 1,000</u>
m) Gain taxed in 1994 [lesser of (g) or (l)]	<u>\$ 1,000</u>

<u>Gain Not Taxed in 1994</u>	
n) Gain realized [(line (g))]	\$10,500
o) Minus: Gain taxed in 1994 [(line (m))]	<u>1,000</u>
p) Gain not taxed in 1994	<u>\$ 9,500</u>

<u>Adjusted Basis of New Home</u>	
q) Cost of new home [(line (k))]	\$64,600
r) Minus: Gain not taxed in 1994 [(line (p))]	<u>9,500</u>
s) Adjusted basis of new home	<u>\$55,100</u>

Trading homes. If you trade your old home for another home, treat the trade as a sale and a purchase.

Example. You owned and lived in a home with a basis of \$41,000. A real estate dealer accepted your old home as a trade-in and allowed you \$50,000 toward a new house priced at \$80,000. You are considered to have sold your old home for \$50,000 and to have had a gain of \$9,000 (\$50,000 – \$41,000). Because you replaced it with a new home costing more than the sales price of the old one, you must postpone the tax on the gain. The basis of your new home is \$71,000 (\$80,000 cost minus \$9,000 gain not currently taxed).

If the dealer had allowed you \$27,000 and assumed your unpaid mortgage of \$23,000 on your old home, \$50,000 would still be considered the sales price of the old home (the trade-in allowed plus the mortgage assumed).

Property used partly as your home and partly for business or rental. You may use part of your property as your home and part of it for business or to produce income. Examples are a working farm on which your house is located, an apartment building in which you live in one unit and rent out the others, or a store building with an upstairs apartment in which you live. If you sell the whole property, you postpone only the tax on the part used as your home. This includes the land and outbuildings, such as a garage for the home, but not those used for the business or the production of income.

When you sell property used as your home and for your business, you should consider the transaction as the sale of two properties. To postpone the gain for the part of the selling price allocated to your home (one property), you must reinvest an amount equal to that part in your new home. The same rule applies if you buy property for use as your home and for your business. Only the part of the purchase price allocated to your home can be counted as the cost of purchasing the new home. See *Investment in a home combined with business or rental property*, later.

Example. You owned a four-unit apartment house. You lived in one unit and rented three units. You sold the apartment house, and you bought and lived in a new home. You did not replace the rental property. Your records show:

Apartment house:	
Cost	\$ 80,000
Capital improvements	20,000
Basis (cost plus improvements)	\$100,000
Minus: Depreciation (on 3 rented units only)	40,000
Adjusted basis	<u>\$ 60,000</u>
Selling price	\$120,000
Selling expenses	\$ 8,000
New home:	
Purchase price	\$ 70,000

Because one-fourth of the apartment building was your home, you figure your postponed gain as follows:

	Personal (1/4)	Rental (3/4)
1) Selling price	\$30,000	\$90,000
2) Selling expenses	2,000	6,000
3) Amount realized (adjusted sales price)	<u>\$28,000</u>	<u>\$84,000</u>
4) Basis (cost plus improvements)	\$25,000	\$75,000
5) Depreciation	—	40,000
6) Adjusted basis	<u>\$25,000</u>	<u>\$35,000</u>
7) Gain [(3) minus (6)]	<u>\$ 3,000</u>	<u>\$49,000</u>
8) Gain not postponed		<u>\$49,000</u>
9) Gain postponed	<u>\$ 3,000</u>	

The gain of \$49,000 on the three-fourths of the building that was rental property is subject to tax in the year of sale. Report this gain on Form 4797, *Sales of Business Property*. You postpone the gain on the one-fourth that was

your home. This is because the \$28,000 adjusted sales price of this one-fourth is less than the \$70,000 cost of your new home. The basis of the new home is \$67,000 (\$70,000 cost minus \$3,000 postponed gain). Report only the part of the sale that represents your main home (one-fourth) on Form 2119.

Business use of your home. If, in the year of sale, you are entitled to deduct expenses for the business use of your home, you cannot postpone the gain on the part of the home used for business. In figuring the amount of gain on which you can postpone tax, you must make an allocation for the part of the home used for business. For information on how to figure the business part, see *Business Part of Home Expenses* in Publication 587.

Example 1. John Daniel is a self-employed music teacher. In 1994 he deducts expenses for the two rooms of his home used for his music lessons and his business office. He sold his home in November at a \$16,000 gain, and he replaced it with a larger, more expensive home that same month.

Because John used his home for business in 1994, he cannot postpone all of his \$16,000 gain on the sale of his home. He must make an allocation similar to that shown in the example under *Property used partly as your home and partly for business or rental*, earlier.

Example 2. Susan Jones bought her home in 1971 for \$40,000. She is a teacher and used part of her den to correct papers and prepare her lessons. She was allowed a deduction for the business use of her home on her tax returns from 1971 through 1975. However, since 1976 she has not taken the deduction because she decided to do her paperwork and lesson preparation at school.

In November 1994, Susan sold her home for \$80,000 and bought a new main home for \$90,000. Because she was not allowed a deduction for the business use of her den on her 1994 return, she does not have to make the allocation. She can postpone the tax on the entire gain on the sale of her old home since she bought a more expensive home within the replacement period.

Note. To figure her gain, Susan must adjust the basis of her old home by depreciation allowed or allowable for the business use of her home from 1971 through 1975.

Home changed to rental property. You cannot postpone tax on the gain on rental property, even if you once used it as your home. The rules explained in this publication generally will not apply to its sale. Gains are taxable and losses are deductible as explained in Publication 527, *Residential Rental Property*. Publication 527 also explains how to figure the basis of this property.

You have not changed your home to rental property if you *temporarily* rented out your old home before selling it, or your new home before living in it, as a matter of convenience or for another nonbusiness purpose. You can postpone the tax on the gain from the

sale if you meet the requirements explained earlier under *Postponement of Gain*.

Example. In January your employer tells you of your transfer to New Jersey in April. You try to sell your home before you leave, but you have not sold it when you move in April. In May you buy a new main home in New Jersey and rent out your old home, while still trying to sell it. In October you sell your old home. Although you temporarily rented out your old home, it is still considered to be your main home. Therefore, you may be able to postpone tax on the gain on the sale of the old home.

For information on how to treat the rental income you receive, see Publication 527.

If you place your home with a real estate agent for rent or sale and it is *not* rented, it is not considered business property or property held for the production of income. The rules explained under *Postponement of Gain* will apply to the sale.

Condemnation. If your home is condemned for public use and you have a gain, you can postpone the tax on the gain in one of two ways. You can postpone the tax under the rules explained in this publication or under the rules for a forced sale by condemnation. The replacement periods may differ for each treatment. You should compare them before deciding which rules to follow.

Condemnations are discussed in Chapter 1 of Publication 544 under *Involuntary Conversions*.

Replacement property. If you treat the transaction as a forced sale, you must buy replacement property that costs at least as much as the amount realized from the forced sale.

Replacement period. For a condemnation, the replacement period begins on the earlier of:

- 1) The date the condemned property was disposed of, or
- 2) The date condemnation was threatened.

The replacement period generally ends 2 years after the close of the first tax year in which you realize any part of the gain on the condemnation.

Example. You are a calendar year taxpayer. You were notified by the city council on March 6, 1992, of its plan to acquire your property, by condemnation if necessary. On June 3, 1994, when your property had an adjusted basis of \$40,000, the city condemned the property and paid you \$50,000. Your replacement period started on March 6, 1992, the date you were notified of the plan to condemn the property. Because you did not dispose of the property until 1994, your replacement period ends on December 31, 1996. This is 2 years after the last day of the year in which you realized the gain.

Gain on casualty. The tax on a gain from a fire, storm, or other casualty cannot be postponed under the rules explained in this publication, but may be postponed under the rules explained in Publication 547, *Nonbusiness Disasters, Casualties, and Thefts*.

Property taxes. You can deduct property taxes as an itemized deduction in the year of sale based on the number of days in the year you owned the property. It does not matter what part of the taxes you actually paid. If the buyer paid delinquent taxes you owed as part of the sale of your home, the payment increases the selling price of your home. The buyer adds the amount paid to his basis in the property. For more information, see Publication 530.

Note: The information reported (generally by the settlement agent) to the IRS and seller of the home on Form 1099-S, *Proceeds From Real Estate Transactions*, must include the part of any real estate tax that is treated as tax imposed on the buyer.

Transfer taxes. You cannot deduct transfer taxes, stamp taxes, and other incidental taxes and charges on the sale of a home as itemized deductions. However, if you pay these amounts as the seller of the property, they are expenses of the sale and reduce the amount you realize on the sale. If you pay these amounts as the buyer, include them in your cost basis of the property.

New Home

Use the **cost of your replacement home** to figure the gain taxed and the gain on which tax is postponed on the sale of your old home. This includes costs incurred within the replacement period (beginning 2 years before and ending 2 years after the date of sale) for the following items:

- 1) Buying or building the home.
- 2) Rebuilding the home.
- 3) Capital improvements or additions.

You cannot consider any costs incurred before or after the replacement period. However, if you are a person outside the U.S. or a member of the Armed Forces, you can include any costs incurred during the suspension period.

New home outside the U.S. If your new home is outside the U.S., you still may be required to postpone your gain from the sale of your old home that is in the U.S. You must buy or build and live in the new home within the time allowed for replacement.

Debts on the new property. The price of a new home includes the debts it is subject to when you buy it (purchase-money mortgage or deed of trust) and the face amount of notes or other liabilities you give for it.

Temporary housing. If a builder gives you temporary housing while your new home is being finished, you must reduce the contract price to arrive at the cost of the new home. To figure the amount of the reduction, multiply the contract price by a fraction. The numerator is the value of the housing, and the denominator is the sum of the value of the housing plus the value of the new home.

Seller-paid points. If you bought your new home after April 3, 1994, you must subtract any seller-paid points from the purchase price in figuring your basis in the home. If you bought your new home after 1990 but before April 4, 1994, and you chose to deduct the seller-paid points, you must reduce your basis in the home by the points the seller paid.

Settlement fees or closing costs. When buying your home, you may have to pay settlement fees or closing costs in addition to the contract price of the property. Some of the settlement fees or closing costs that you can include in the basis of your property are:

- 1) Abstract fees (sometimes called abstract of title fees),
- 2) Charges for installing utility services,
- 3) Legal fees (including title search and preparing documents),
- 4) Recording fees,
- 5) Surveys,
- 6) Transfer taxes,
- 7) Title insurance, and
- 8) Any amounts the seller owes that you agree to pay, such as back taxes or interest, recording or mortgage fees, charges for improvements or repairs, and sales commissions.

Settlement fees do not include amounts placed in escrow for the future payment of items such as taxes and insurance.

If you itemize your deductions in the year you buy the house, you can deduct some of the costs you paid at closing, such as real estate taxes, mortgage interest, and "points" that are deductible as interest. You may also be able to deduct points paid by the seller at closing. For more information, see Publication 936 and Publication 530.

Real estate taxes. If you agree to pay taxes the seller owed on your new home (that is, taxes up to the date of sale), the taxes you pay are treated as part of the cost. You cannot deduct them as taxes paid. If the seller paid taxes for you (that is, taxes beginning with the date of sale), you can still deduct the taxes. If you do not reimburse the seller for your part of the taxes, you must reduce your basis in your new home by the amount of those taxes. For more information, see *Settlement or closing costs* under *Basis* in Publication 530.

Note: The information reported (generally by the settlement agent) to the IRS and seller of home on Form 1099-S, *Proceeds From Real Estate Transactions*, must include the part of any real estate tax that is treated as tax imposed on the buyer. See *Property taxes* under *Old Home*, earlier.

You cannot deduct, or add to your basis, certain settlement fees or closing costs. These include fire insurance premiums, mortgage insurance premiums, charges for the use of utilities, rent for occupancy before closing, and other fees or charges for services concerning occupancy of the house.

Investment in retirement home. You have not purchased a replacement home if you sell your home and invest the proceeds in a retirement home project that gives you living quarters and personal care but does not give you any legal interest in the property. Therefore, you must include in income any gain on the sale of your home. However, if you are 55 or older, see *Exclusion of Gain*, later.

Allocation between you and your spouse.

You or your spouse may have owned the old home separately, but title to the new one is in both your names as joint tenants. Or, you and your spouse may have owned the old home as joint tenants, and either you or your spouse owns the new home separately. In both of these cases, you can postpone the gain from the sale of the old home.

You and your spouse can divide the postponed gain, which reduces the basis of the new home, if both of you meet the following requirements:

- 1) You used the old home as your main home and you use the new home as your main home.
- 2) You sign a statement that says: "We agree to reduce the basis of the new home by the gain from selling the old home."

Both of you must sign the statement. You can make the statement in the bottom margin of Form 2119 or on a sheet attached to your tax return. If both of you do not sign the statement, you must report the gain in the regular way without allocation.

Example 1. You sell your home that is owned separately by you, but both you and your spouse use it as your main home. The adjusted sales price is \$98,000, the adjusted basis is \$86,000, and the gain on the sale is \$12,000. Within 2 years you and your spouse buy a new home for \$100,000. The title is held jointly, and under state law, you each have a one-half interest. If you both sign the statement to reduce the basis of the new home, you postpone the gain on the sale as if you had owned both the old and new homes jointly. You and your spouse will each have an adjusted basis of \$44,000 (\$50,000 cost minus \$6,000 postponed gain) in the new home.

If you both do not sign the statement, your entire gain of \$12,000 will be currently taxed. This is because the adjusted sales price of the old home (\$98,000) is greater than your part of the cost of the new home (\$50,000). You and your spouse will each have a basis of \$50,000 in the new home.

Example 2. Assume in Example 1 that you and your spouse owned the old home jointly and each had a one-half interest under state law. Your spouse buys the new home with separate funds and takes title individually. If you both sign the statement, you and your spouse postpone the \$12,000 gain from the sale of the old home. Your spouse will have an adjusted basis of \$88,000 (\$100,000 cost minus \$12,000 postponed gain) in the new home.

If you both do not sign the statement, you will be taxed on your share of the gain on the old home, but your spouse will postpone tax on his or her share of the gain. This is because the cost of the new home was more than your spouse's share of the adjusted sales price of the old home. Your spouse's basis in the new home will be \$94,000 (\$100,000 cost minus \$6,000 postponed gain).

Example 3. Assume in Example 1 that you own the old home individually and your spouse owns the new home individually. If you both sign the statement, you postpone the \$12,000 gain from the sale of the old home. Your spouse will have an adjusted basis in the new home of \$88,000.

If you both do not sign the statement, your entire gain will be taxed, and your spouse's basis in the new home will be \$100,000.

Deceased spouse. If your spouse dies after you sell your old home and before you purchase a new home, you can postpone the gain from the sale of the old home if the basic requirements are met, and:

- 1) You were married on the date your spouse died, and
- 2) You use the new home as your main home.

This applies whether title to the old home is in one spouse's name or held jointly.

If you sold your home and did not postpone the entire gain on the sale because of the death of your spouse (but otherwise qualified to do so under the rules explained in this publication), you can file an amended return (Form 1040X) to postpone the entire gain. See *Time to exclude gain under How to Make and Revoke a Choice to Exclude Gain* for information about the time allowed to file an amended return.

Separate homes replaced by single home.

If you and your spouse had two separate gains from the sales of homes that had been your separate main homes before your marriage, you may have to postpone the tax on both gains. This can happen if you jointly purchase a new replacement home and one-half the amount of the cost of the new home is at least as much as the adjusted selling price of each of your old homes.

Each spouse must individually satisfy the requirements for postponing gain. Each spouse's share of the cost of the new home is the portion equal to his or her interest in the home under state law (generally one-half). This share of the cost must be equal to or greater than the adjusted sales price of his or her old home.

Example. You sold your old home in April 1994 for an adjusted sales price of \$90,000. Your spouse sold her old home in June 1994 for an adjusted sales price of \$110,000. You each realized a gain from your sale. Before the end of 1994, you jointly purchased a new replacement home at a cost of \$200,000. Under state law, you each have a one-half interest in the new home.

You must postpone your gain since you are treated as purchasing a replacement home for \$100,000 (½ of \$200,000).

There is tax on \$10,000 of your spouse's gain at the time of the sale. This is the amount by which the adjusted sales price of her former home is more than her \$100,000 share of the cost of the replacement home.

Report the sales of the old homes on separate Forms 2119.

Title to new home not held by either you or your spouse.

You cannot postpone the tax on the gain from the sale of your old home if you reinvest the proceeds from the sale in a new home in which neither you nor your spouse holds any legal interest. For example, if someone else (such as your child) holds the title to the new home, you cannot postpone the gain from the sale.

Home replaced by two homes of spouses living apart.

If you and your spouse have agreed to live apart, and you each buy and live in separate replacement homes, the postponement provisions apply separately to your gain and to your spouse's gain.

Example. You and your spouse bought a home in 1984. You owned the property jointly and used it as your main home. In 1994 you agreed to live apart and sold the home for \$98,000. The gain on the sale was \$20,000. Under state law, each of you is entitled to one-half of the proceeds of the sale. Therefore, each of you had a \$10,000 gain from the sale of your home.

Before the end of 1994 you and your spouse individually bought and lived in separate homes. The cost of each new home, \$71,000 and \$75,000 respectively, was more than your respective shares of the adjusted sales price of the old home. You and your spouse must postpone the tax on the \$20,000 gain on the old home.

Your new home has an adjusted basis of \$61,000 (\$71,000 minus ½ of \$20,000 gain postponed). Your spouse's new home has an adjusted basis of \$65,000 (\$75,000 minus ½ of \$20,000 gain postponed).

You report the sale of your home on two Forms 2119 as if two separate properties were sold. You each report half of the sales price. See *Divorce after sale under How and When to Report*, later.

Investment in a home combined with business or rental property.

If you replace your old home with property used partly as your home and partly for business or rental, you consider only the cost of the part used as your home in determining the cost of your replacement home. You must compare the cost of this part to the adjusted sales price of the old home to determine the amount of gain taxed in the year of sale and the amount of gain on which tax is postponed.

Example. Your old home had a basis of \$50,000. You sold it in September for an adjusted sales price of \$75,000. Your gain is \$25,000. In October, you bought a duplex house for \$120,000. You live in half and rent

the other half. Because only half of the cost of the duplex (\$60,000) is considered an investment in a new main home, the amount of the proceeds not reinvested in a home is \$15,000 (\$75,000 – \$60,000). Therefore, you are taxed on \$15,000 of the \$25,000 gain on the sale. You must postpone tax on \$10,000 of the gain reinvested in your new home. The basis of your new home is \$50,000 (\$60,000 cost minus \$10,000 postponed gain). The basis of the rented part of the duplex is \$60,000.

Inheritance or gift. If you receive any part of your new home as a gift or an inheritance, you cannot include the value of that part in the cost of the new home when figuring the gain taxed in the year of sale and the gain on which tax is postponed. However, you include the basis of that part in your adjusted basis to determine any gain when you sell the new home.

Example. Your father died in 1994 and you inherited his home. Its basis to you is \$62,000. You spent \$14,000 to modernize the home, resulting in an adjusted basis to you of \$76,000.

When your father died, you owned a home that you bought in 1989 for \$60,000. Assume that within 2 years of inheriting your father's home you sell your old home for \$65,000, at a gain of \$5,000. You have fixing-up expenses of \$200 on your old home.

To find the gain taxed in the year of the sale, you compare the adjusted sales price of the old home, \$64,800 (\$65,000 – \$200), with the \$14,000 you invested in your new home. The \$5,000 gain is fully taxed because the adjusted sales price of the old home is more than the amount you paid to remodel your new home. For this purpose, you do not include the value of the inherited part of your property (\$62,000) in the cost of your new home.

Holding period. If you postpone tax on any part of the gain from the sale of your old home, you will be considered to have owned your new home for the combined period you owned both the old and the new homes.

More than one main home bought or sold in a 2-year period.

If you buy or build more than one main home during the replacement period, only the last one can be treated as your **new main home** to determine whether you must postpone the gain from the sale of the old home.

If you postponed the gain on the sale of your old home, then sell your new home within 2 years after the sale of your old home, you generally cannot postpone the gain on the sale of the new home.

The following examples illustrate these rules.

Example 1. You sold your first home in March 1993 for \$120,000, and you had a \$10,000 gain on the sale. You postponed the \$10,000 gain because you bought a second home in April 1993 for \$135,000. Your basis in the second home, as reported on the Form 2119 filed with your 1993 return, was \$125,000 (\$135,000 cost less the \$10,000 postponed gain).

In June 1994 you sold the second home for \$142,000 and you moved into an apartment. You purchased a third home in January 1995 for \$146,000.

Your replacement home for the first home you sold (in March 1993) is the last main home you bought in the following 2-year period. This is the third home you bought (in January 1995). Since its \$146,000 cost is more than the \$120,000 sales price of your first home, your \$10,000 gain is postponed. Your basis in your third home is \$136,000 (\$146,000 cost less the \$10,000 postponed gain). You must file a new Form 2119 for 1993 to change the information you gave about your replacement home.

You cannot postpone the gain on the June 1994 sale of your second home. This is because it was within 2 years after the March 1993 sale of your first home on which you postponed the gain. Since you no longer treat your second home as the replacement for your first home, the basis of your second home is its \$135,000 cost. You must include the \$7,000 gain on its sale (\$142,000 sales price less the \$135,000 basis) in your 1994 income.

Example 2. Assume the same facts as in Example 1 except you purchased your third home in September 1995 rather than in January. Your second home is the replacement home for your first home (sold in March 1993). This is because it was the only home bought in the following 2-year period.

Although you bought another new main home within 2 years after selling your second home, you cannot postpone the gain on the June 1994 sale of your second home. This is because its sale was within 2 years of the March 1993 sale of your first home. You must report the \$17,000 gain on the June 1994 sale of your second home (\$142,000 sales price minus \$125,000 basis) on your 1994 tax return. Your basis in your third home (that you bought in September 1995) is its cost, \$146,000.

Exception. The rules for more than one home bought or sold in a 2-year period do not apply if you sell your main home because of a **work-related move**. A "work-related move" is one for which you are allowed a deduction for moving expenses. To qualify for the deduction, the move must be closely related to the start of work, and you must meet the time and distance requirements explained in Publication 521.

If the exception applies, treat each sale as though the 2-year rule did not apply.

Example. You sell two homes within 2 years as shown below:

January 1994	You sell your house in Chicago at a gain.
February 1994	You buy a more expensive house in Memphis .
March 1995	You sell your house in Memphis due to a transfer required by your employer.
March 1995	You buy a more expensive house in New York City . The move meets the requirements for a moving expense deduction.

When you complete the 1994 Form 2119 for the sale of your house in Chicago, compare the cost of the home bought in Memphis with the adjusted sales price of the house in Chicago, even though you bought another new main home within 2 years (New York City in March 1995).

Your 1995 Form 2119 will compare the adjusted sales price of the house in Memphis (sold March 1995) with the cost of the house in New York City.

Continue to postpone gain. If you bought your present home and postponed tax on gain from a prior sale under the postponement-of-gain rules discussed earlier, you continue to postpone the tax if you replace your present home under those rules.

Example. In 1975 you sold your home, which you had owned since 1965, and bought a new one. The tax on the gain was postponed and the basis of the home you bought in 1975 was reduced by the gain you postponed. This year you sold the home you bought in 1975 and bought a more expensive one. You must postpone tax on the gain from selling the home you bought in 1975.

How and When to Report

If you sold your home during the year, report the details of the sale as explained in this section. Report the sale even if you have a loss, you postponed the tax on the entire gain, or you have not purchased a new home.

Form 2119. Use Form 2119, *Sale of Your Home*, to report the sale of your old home and any purchase of a new one. File Form 2119 for the year you sold your old home. You may also have to file a second Form 2119 when you purchase your new home. Several filled-in Forms 2119 are shown at the end of this publication.

Keep a copy of Form 2119 with your tax records for the year. Form 2119 is also a supporting document that shows how your new home's basis is decreased by the amount of any postponed gain on the sale of your old home. Therefore, you should also keep a copy of Form 2119 with your records for the basis of your new home.

Reporting a loss. You must report the sale of your main home even if you have a loss on the sale. Complete Part I of Form 2119 for the year in which the sale occurred. The loss does not reduce your income.

If you report a loss on the sale, you do not have to file a second Form 2119 if you later purchase a new home. The loss on the sale has no effect on the basis of your new home.

Schedule D (Form 1040). If you report taxable gain on the sale of your main home, you will also have to file a Schedule D (Form 1040), *Capital Gains and Losses*, with your return.

Maximum tax rate on capital gains. Your net capital gain is taxed at a maximum tax rate of 28%, even if you have ordinary income that is taxed at a higher rate. If you have net capital gains and your taxable income is taxed at a rate higher than 28%, figure your tax using the

Capital Gain Tax Worksheet in the Form 1040 instructions.

New home purchased before return filed. If you buy a new home before you file a return for the year of sale of your old home, complete Form 2119 and attach it to your return.

Reporting a gain. If your new home costs as much as or more than the adjusted sales price of your old home, you postpone the tax on the entire gain. You do not need to report the sale on Schedule D (Form 1040).

If the new home costs less than the adjusted sales price of the old home, the gain is taxed to the extent of the difference. Report the taxable gain on Schedule D (Form 1040) for the year of sale.

New home not yet purchased. If you plan to replace your home but have not done so by the time your return for the year of sale is due, you must still report the sale. Complete Form 2119, Part I only, and attach it to your return for the year of sale.

If you do not plan to replace your home within the replacement period, you must still complete Form 2119 and attach it to your return for the year of sale. If you have a gain on the sale, you will also need to complete Schedule D (Form 1040) and attach it to your return.

New home purchased after return filed. If you postponed gain from the sale of your old home and you buy and live in a new home after you file your return but within the replacement period, you should notify the IRS. File a second Form 2119 giving the date you first lived in the new home and its cost.

If you paid tax on the gain from the sale of your old home, but replaced it within the replacement period, see *Home replaced after tax paid on gain*, later.

New home costs at least as much as adjusted sales price. If you postponed gain from the sale of your old home, and your new home costs at least as much as the adjusted sales price of your old home, file a second Form 2119 by itself. Your address, signature, and the date are required on this Form 2119. If you filed a joint return for the year of sale, both you and your spouse must sign the Form 2119. File it with the Director of the Internal Revenue Service Center where you would file your next tax return.

New home costs less. If you postponed gain from the sale of your old home, and your new home costs less than the adjusted sales price of the old home, you must file an amended return (Form 1040X) for the year of the sale. Attach a second completed Form 2119 and Schedule D (Form 1040) showing the gain you must report. You will have to pay interest on any additional tax due on the amended return. The interest is generally figured from the due date of the return for the year of sale.

Old home not replaced or new home not purchased within replacement period. If you do not plan to replace your old home, you must complete Form 2119 and Schedule D (Form 1040) to report any gain. Attach them to

your tax return for the year of the sale. The entire gain is taxable unless you are eligible to exclude all or part of the gain. See *Exclusion of Gain*, later.

You may have postponed gain on the sale of your old home because you planned to replace it. If you do not replace it within the replacement period, you will have to file a second Form 2119. Attach it to an amended return (Form 1040X) for the year of the sale. Include a Schedule D (Form 1040) to report your gain and any other appropriate schedule. For example, you would have to include Form 6252 to report an installment sale. You will have to pay interest on the additional tax due on the amended return. The interest is generally figured from the due date of the return for the year of sale.

Divorce after sale. If you are divorced after filing a joint return on which you postponed the gain on the sale of your home, but you do not use your share of the proceeds to buy or build a new home (and your former spouse does), you must file an amended joint return to report the tax on your share of the gain. If your former spouse refuses to sign the amended joint return, attach a letter explaining why your former spouse's signature is missing.

Home replaced after tax paid on gain. If you paid tax on the gain from the sale of your old home, and you buy and live in a new home within the replacement period, you must file an amended return (Form 1040X) for the year of sale of your old home. Complete a new Form 2119 and include it with your amended return. Report on Schedule D (Form 1040) any gain on which you cannot postpone the tax, and claim a refund of the rest of the tax.

Installment sale. Some sales are made under arrangements that provide for part or all of the selling price to be paid in a later year. These sales are called "installment sales." If you finance the buyer's purchase of your home yourself, instead of having the buyer get a loan or mortgage from a bank, you may have an installment sale. If the sale qualifies, you can report the part of the gain you cannot postpone on the installment basis.

Seller-financed mortgage. If you sell your home and hold a note, mortgage, or other financial agreement, the payments you receive generally consist of both interest and principal. You must report the interest you receive as part of each payment separately as interest income. If the buyer of your home uses the property as a personal residence, you must also report the name, address, and social security number of the buyer on line 1 of either Schedule B (Form 1040) or Schedule 1 (Form 1040A). The buyer must give you his or her social security number and you must give the buyer your social security number. Failure to meet these requirements may result in a \$50 penalty for each failure. For more information, see Publication 537, *Installment Sales*.

Statute of limitations. The 3-year limit for assessing tax on the gain from the sale of your

home begins when you give the IRS information that shows that:

- 1) You replaced your old home, and how much the replacement home cost,
- 2) You do not plan to buy a new home within the replacement period, **or**
- 3) You did not buy a new home within the replacement period.

This information may be on the Form 2119 attached to your tax return for the year of the sale, or on a second Form 2119 filed later. File the second Form 2119 with the Service Center where you will file your next tax return. If needed, send an amended return for the year of the sale to include in income the gain that you cannot postpone.

Example

Frank and Evelyn Harris bought a new home and moved in on May 4, 1994. Their old home, which they purchased in 1979, was sold at a gain on May 6, 1994. The price of the new home was less than the adjusted sales price of the old home. In 1994 they must include in income the difference between the cost of the new home and the adjusted sales price of the old home. Neither Frank nor Evelyn was 55 or older on the date of the sale.

They report the sale on Form 2119 and include the taxable part of the gain on Schedule D (Form 1040). A filled-in Form 2119 showing this example appears later in this publication.

Frank and Evelyn's records show the following:

1) Original cost of old home (including settlement costs)	\$58,500
2) Improvements to old home (new porch, trees, fence)	4,500
3) Fixing-up expense (painting)	500
4) Selling price of old home	87,000
5) Commission paid on sale	5,200
6) Balance of mortgage on old home ...	38,000
7) Interest on old mortgage from 5/1/94 to 5/5/94, charged at settlement	53
8) 1994 real estate taxes on old home	860
9) Real estate taxes from 1/1/94 to 5/5/94 paid to buyer of old home	299
10) Refund of insurance on old home	40
11) Purchase price of new home	76,200
12) Title search and settlement costs of new home	1,000
13) 1994 real estate taxes on new home	975
14) Real estate taxes from 1/1/94 to 5/3/94 received from seller of new home	210
15) 1 year's fire insurance paid in advance on new home	200
16) Mortgage on new home	47,500

Frank and Evelyn use some items from their records to figure the gain on the sale of their old home or the adjusted basis of their new home. They use other items to figure the deductions allowable on Schedule A (Form 1040). Others they cannot use at all. For information on how to treat the mortgage interest and real estate taxes, see Publications 530 and 936.

They figure the gain on the sale of their old home, the part of the gain on which tax is postponed and the part on which it is not, and the adjusted basis of their new home in the following way (the items referred to appear in the preceding list):

<u>Gain Realized</u>	
a) Selling price of old home (item 4)	\$87,000
b) Minus: Selling expenses (item 5)	5,200
c) Amount realized on sale ...	\$81,800
d) Minus: Adjusted basis of old home (items 1 and 2)	63,000
e) Gain realized	<u>\$18,800</u>

<u>Gain Taxed in 1994</u>	
f) Amount realized on sale ...	\$81,800
g) Minus: Fixing-up expenses (item 3)	500
h) Adjusted sales price	\$81,300
i) Minus: Cost of new home (items 11 and 12)	77,200
j) Excess of adjusted sales price over cost of new home	<u>\$ 4,100</u>
k) Gain taxed in 1994 [lesser of (e) or (j)]	<u>\$ 4,100</u>

<u>Gain Not Taxed in 1994</u>	
l) Gain realized [line (e)]	\$18,800
m) Minus: Gain taxed in 1994 [line (k)]	4,100
n) Gain not taxed in 1994	<u>\$14,700</u>

<u>Adjusted Basis of New Home</u>	
o) Cost of new home [line (i)]	\$77,200
p) Minus: Gain not taxed in 1994 [line (n)]	14,700
q) Adjusted basis of new home	<u>\$62,500</u>

Frank and Evelyn attach Form 2119 to their return showing this information. They also enter \$4,100, the part of the gain taxed in 1994, on line 12 of Schedule D (Form 1040).

Exclusion of Gain

Words you may need to know (see Glossary):

Main home
One-time exclusion

This section discusses how to exclude from gross income all or part of your gain from the sale of your main home if you meet certain age, ownership, and use tests at the time of the sale. This is a one-time exclusion of gain for sales after July 26, 1978.

The decision of when to take the exclusion depends on many factors. You will want to consider your personal tax and financial situation before deciding when to make the choice.

If you meet the requirements discussed in this section and you make the choice to exclude gain on the sale of your main home, the excluded gain is not taxed.

If you change your mind after you file the return for the year of sale, you may be able to make or revoke the choice later. You would have to file an amended return for the year of sale within certain time limits. See *How to Make and Revoke a Choice to Exclude Gain*, later.

Exclusion Amount

If you meet the age, ownership, and use tests, you can choose to exclude \$125,000 of your gain on the sale of your home. If you are married on the date of the sale and file a separate return, you can choose to exclude only \$62,500. Your gain is the amount realized on the sale minus the adjusted basis of the home. If there is gain remaining after the exclusion, you may be required to postpone tax on the rest of the gain if, as explained earlier, you buy and live in another home.

Age, Ownership, and Use

You can choose to exclude from income \$125,000 of gain (\$62,500 if you were married on the date of sale and file a separate return) if you meet **all** the following requirements.

- 1) You were **55 or older** on the date of the sale.
- 2) During the **5-year period** ending on the date of the sale, you:
 - **Owned** your main home for at least **3 years**, and
 - **Lived in** your main home for at least **3 years**.
- 3) You or your spouse have never excluded gain on the sale of a home after July 26, 1978. However, see *Effect of Marital Status*, later, for more details.

Age 55 at time of sale. You must be 55 by the date you sell the home to qualify for the exclusion. You do not meet the age 55 test if you sell the property during the year in which you will be 55 but before you actually become 55. The earliest date on which you can sell your home and still qualify for the exclusion is your 55th birthday.

Ownership and use tests. The required 3 years of ownership and use (during the 5-year period ending on the date of the sale) do not have to be continuous. You meet the tests if you can show that you owned and lived in the property as your main home for either 36 full months or 1,095 days (365 × 3) during the 5-year period. Short temporary absences for vacations or other seasonal absences, even if you rent out the property during the absences, are counted as periods of use. See *Ownership and use tests met at different times*, later.

Example 1. From 1987 through 1991 Joseph Mooney lived with his son and daughter-in-law in a house owned by his son. On January 5, 1992, he bought this house from his son. He continued to live there until May 29, 1994,

when he sold it. Although Joseph **lived in** the property as his main home for more than 3 years, he cannot exclude his gain on the sale. This is because he did not **own** the property for the required 3 years.

Example 2. Professor John Thomas bought and moved into a house on January 4, 1991. He lived in it as his main home continuously until February 1, 1993, when he went abroad for a 1-year sabbatical leave. During part of the period of leave, the property was unoccupied, and during the rest of the period, he rented it out. On March 4, 1994, he sold the house. Because his leave was not a short temporary absence, he cannot include the period of leave to meet the test of living in the house as his main home for 3 years or more. He cannot exclude his gain from income because he did not live in the house for the required period.

More than one owner. If a husband and wife sell their jointly owned home and either one meets the age, ownership, and use tests, both are considered to have met the tests. See *Jointly owned home*, later.

If the joint owners of a home are other than husband and wife, each owner who chooses to exclude gain from income must meet the age, ownership, and use tests. If one owner meets the tests, that does not automatically qualify the other owners to exclude their gain from income. Each owner excludes gain on an individual basis. A choice by one owner does not keep the other owners from making a choice when they sell a different home in the future.

Example. Frank Smith and his sister, Mary, each own a one-half interest in their jointly owned home. Frank meets the age, ownership, and use tests, but Mary does not. The adjusted basis of the home is \$28,000, or \$14,000 each. They sell the home for \$180,000. Frank's interest in the amount realized is \$90,000 ($\frac{1}{2} \times \$180,000$). He can choose to exclude from gross income his entire gain of \$76,000 (\$90,000 minus \$14,000). Mary must postpone tax on her \$76,000 gain if she meets the requirements explained earlier under *Postponement of Gain*. If not, she must include her gain in income for the year of sale.

Previous home destroyed or condemned. For the ownership and use tests, you add the time you owned and lived in a previous home that was destroyed or condemned to the time you owned and lived in the home on which you wish to exclude gain. This rule applies if any part of the basis of the home you sold depended on the basis of the destroyed or condemned home. Otherwise, you must have owned and lived in the **same** home for 3 of the 5 years before the sale to qualify for the exclusion.

Ownership and use tests met at different times. You can meet the ownership and use tests during different 3-year periods. However, you must meet both tests during the 5-year period ending on the date of the sale.

Example. In 1987, Grace Jones was 50 years old and lived in a rented apartment. The

apartment building was later changed to a condominium and she bought her apartment on December 1, 1990. In 1992, Grace became ill and on April 14 of that year she moved to her daughter's home. On February 14, 1994, while still living in her daughter's home, she sold her apartment.

Grace can exclude the gain on the sale of her apartment because she met the age, ownership, and use tests. Grace was over 55 at the time of the sale. Her 5-year period is from February 15, 1989, to February 14, 1994, the date she sold the apartment. She owned her apartment from December 1, 1990, to February 14, 1994 (over 3 years). Grace lived in the apartment from February 15, 1989, to April 14, 1992 (over 3 years).

Exception for disabled individual. There is an exception to the 3 of 5-year use test if you become physically or mentally unable to care for yourself at any time during the 5-year period. This exception applies to sales made after September 30, 1988.

You qualify for this exception to the use test if, during the 5-year period before the sale of your home:

- 1) You owned and lived in your home as your main home for a total of at least 1 year, and
- 2) You became physically or mentally unable to care for yourself.

Under this exception, you are considered to live in your home during any time that you reside in a facility (including a nursing home) that is licensed by a state or political subdivision to care for persons in your condition.

Jointly owned home. Both you and your spouse will meet the age, ownership, and use tests if you meet **all** of the following requirements.

- 1) You hold the home either as joint tenants, tenants by the entirety, or community property on the date of the sale.
- 2) You file a joint return for the tax year in which you sell the home.
- 3) Either you or your spouse is 55 or older on the date of sale and has owned and lived in the property as a main home for the required time before the sale.

Home of spouse who died. You will meet the ownership and use tests if your spouse is deceased on the date you sell your main home, and:

- 1) You have not remarried,
- 2) Your deceased spouse had met the ownership and use tests for that main home, and
- 3) Your deceased spouse had not previously chosen or joined in choosing to exclude gain on the sale of another main home after July 26, 1978.

You must still meet the age test (be at least age 55 on the date of sale) to qualify for the exclusion.

Example. Ellen and Doug Smith were married January 6, 1992. After their marriage, their main home was property Doug had owned and lived in as his main home since January 2, 1982. Doug died on January 2, 1994, and he had never chosen or joined in choosing to exclude gain on the sale of any home.

Ellen inherited the property and continued to live in it as her main home until December 10, 1994, when she sold it. At the date of sale she was 56 years old, had not remarried, and had never chosen or joined in choosing to exclude gain on the sale of any home. Ellen can choose to exclude up to \$125,000 of the gain from the sale of her home. This is because she meets the age test and Doug met the 3 of 5-year ownership and use tests for the property.

Sale by executor. Gain from the sale of a home by the executor of an estate may qualify for this exclusion. To qualify, the sale must be made under a contract entered into before death by a taxpayer who met the age, ownership, and use tests.

Rent-controlled apartment. If you receive a payment to give up your rights in a rent-controlled apartment, this gain does not qualify for the exclusion. You do not meet the ownership test when you rent an apartment.

Main Home

Main home has the same meaning for the exclusion of gain as it has for postponing tax on gain. See *Main Home* under *Postponement of Gain*, earlier.

Part of property used as main home. You may use only part of the property as your main home, as explained earlier under *Old Home* and its discussion, *Property used partly as your home and partly for business or rental*. In this case, the rules discussed in this section of the publication apply only to the gain on the part of the property used as your main home.

Example. Dr. Martin Russell met the age, ownership, and use tests when he sold his main home. However, for the whole time he owned the home, he used half of it exclusively as an office for treating his patients. Only the half of the property used as his home qualifies for the choice to exclude gain from gross income. This is because Dr. Russell did not use the whole property as his main home.

For an example of how to divide the gain between the part of the property used as your home and the part used for business or other purposes, see *Property used partly as your home and partly for business or rental*, earlier.

Note: If the business use of your old home did not exceed 2 years of the 5-year period ending on the date of the sale, you do not have to divide the gain. However, you must decrease your basis in the old home by the depreciation allowed or allowable for the business use of it. See *Adjusted Basis*, earlier.

Home traded. If you trade your old home for a different home, the trade is treated as a sale

and a purchase. Gain on the old home may qualify for exclusion from gross income. See *Trading homes*, under *Old Home*, earlier.

Land. If you sell the land on which your main home is located, but not the house itself, you cannot exclude from income any gain you have from the sale of the land.

Home on condemned property. If your home is condemned for public use, you can treat the transaction as a sale of the home. If you choose to exclude gain from the condemnation, you must follow the rules explained earlier in this section. If you have any gain remaining after the exclusion, you may have to postpone the tax on the rest of the gain as explained earlier under *Postponement of Gain*. Or, you can postpone it under the rules for a condemnation, as explained under *Involuntary Conversions* in Publication 544.

Damage to home. If your home is damaged by fire, storm, or other casualty, you can choose to exclude gain from insurance proceeds or other compensation. You must follow the rules explained earlier in this section. However, you cannot postpone the tax on the rest of the gain by using the rules explained earlier under *Postponement of Gain*. The rest may qualify, however, under the postponement-of-gain rules explained in Publication 547, *Non-business Disasters, Casualties, and Thefts*.

Effect of Marital Status

For purposes of the exclusion, your marital status is determined as of the date of sale of your home. If you are legally separated under a decree of divorce or of separate maintenance, you are not considered married.

Married persons. If you are married when you sell your main home, you cannot choose to exclude the gain unless your spouse joins you in making the choice. Your spouse must join you in the choice even if:

- 1) You or your spouse owned the home separately,
- 2) You and your spouse file separate returns, or
- 3) The spouse not owning an interest in the home had not lived in it for the required period before the sale.

If your spouse died after the sale, but before making the choice to exclude the gain, his or her personal representative (administrator or executor, for example) must join with you in making the choice. You, as the surviving spouse, are considered the personal representative of your deceased spouse if no one else has been appointed.

If the home is not jointly owned, the spouse who owns the property must meet the age, ownership, and use tests. The other spouse must join in making the choice.

Separate return. If you are married on the date of sale, file a separate return, and meet

the age, ownership, and use tests, you can exclude no more than \$62,500 of gain on the sale of your main home. Your spouse must show agreement to your choice by writing in the bottom margin of Form 2119, or on an attached statement, "I agree to the Part II election," and signing his or her name.

You or your spouse can exclude gain only once. If you or your spouse chooses to exclude gain from a sale after July 26, 1978, neither of you can choose to exclude gain again for a sale after that date. If you and your spouse each owned separate homes before your marriage and sold both homes after your marriage, you can exclude the gain on one of them, but not on both. If after choosing to exclude gain, you and your spouse divorce, neither of you can exclude gain again. If you remarry, you and your new spouse cannot exclude gain on sales after your marriage. However, you can revoke a previous choice as discussed later under *How to Make and Revoke a Choice to Exclude Gain*.

Marital status on date of sale. Your marital status on the date of the sale determines the amount you can exclude, whether your spouse must join you in the election to exclude gain, and whether each spouse can make his or her own election later.

Sale before marriage. If you meet the age, ownership, and use tests when you sell your separately owned home during the year, you can exclude gain up to \$125,000. If you marry before the end of the year, you can take the exclusion whether you file a joint return or a separate return. This is because you were single on the date of the sale.

If one spouse sells a home before the marriage, the other spouse is not required to join in the election to exclude gain. The spouse who did not join in the election is eligible to make an election if he or she later sells a house, meets the age, ownership, and use tests, and is single or married to a different spouse who has never made or joined in an election.

If one spouse makes an election to exclude up to \$125,000 of the gain from a house sold before marriage, that spouse cannot join in another election to exclude gain. If this couple then sells a home during their marriage, neither can exclude any gain. This is because both spouses are required to join in the election, and one spouse has already excluded gain.

Example 1. Tom Oak sold his main home in January 1992. He met the age, ownership, and use tests to exclude gain on the sale. In June 1992, he married Susan Green. They filed a joint return for 1992 and Tom elected to exclude the gain on the sale of his house. Susan was not required to join in Tom's election since they were not married on the date of the sale.

While married, Tom and Susan lived in Susan's separately owned house. Tom died in 1994 and Susan sold her house shortly after Tom's death. She met the age, ownership, and use tests to exclude gain on the sale. She can exclude up to \$125,000 of the gain. This is because she was single on the date of sale and

she has never made an election to exclude gain before. She was not required to join in Tom's election.

Example 2. Frank and Sheila Brown were married in 1987. In January 1993, they sold their jointly owned home. Frank and Sheila met the age, ownership, and use tests, so they chose to exclude their gain of \$70,000 on their joint return for 1993. The Browns divorced in February 1994.

In July 1994, Sheila married Mike Jones. Mike had sold his home in March 1994 when he was single. He met the age, ownership, and use tests at the time of sale. Mike can choose to exclude up to \$125,000 gain on a separate or joint return because he was single at the time he sold his home. This is so even though Sheila joined Frank in choosing to exclude gain.

Example 3. Joe Johnson and Betty Smith were single and each owned a home. In August 1994, they sold their homes and each had a gain of \$125,000, for a total gain of \$250,000. Each met the age, ownership, and use tests at the time of sale.

In October 1994, Joe and Betty married. Because Joe and Betty were single when they sold their homes, they each can choose to exclude \$125,000 of gain (\$250,000 total). This is true whether they file a joint return or separate returns.

Example 4. In February 1994, Bill and Sally White were divorced. At that time they had their jointly owned home up for sale. Sally married Ken Brown in November 1994. In December 1994, Bill and Sally sold their home at a gain. Because Bill and Sally were not married to each other at the time they sold their home and they each met the tests to exclude gain, each can choose to exclude up to \$125,000 gain based on the part of the home each owned. (See *Example* under *Age, Ownership, and Use* and its discussion, *More than one owner*, earlier.)

Sally files a joint return and chooses to exclude up to \$125,000 of her part of the gain. Ken must join Sally in her choice. Bill files a single return and chooses to exclude up to \$125,000 of his gain.

If Ken Brown later sells a home, he cannot choose to exclude gain because he was required to join Sally in her choice. Ken is considered to have made a lifetime choice.

Example 5. David and Beth Pine sell their jointly owned home. They both meet the ownership and use tests at the time of sale, but David is 62 and Beth is 50. They file separate returns for the year they sell their house. Because Beth does not meet the age test, she cannot choose to exclude gain on her separate return. David can choose to exclude up to \$62,500 of the gain on his separate return only if Beth joins him in making his choice.

If Beth did join David in making his choice and she later sells a home, she cannot choose to exclude gain because she joined David in his choice.

How to Make and Revoke a Choice to Exclude Gain

You can exclude gain on the sale of your main home **only once** for sales after July 26, 1978.

Time to exclude gain. You can make or revoke a choice to exclude gain from a particular sale at any time before the **latest** of the following dates.

- 1) Three years from the due date of the return for the year of the sale.
- 2) Three years from the date you filed the return.
- 3) Two years from the date you paid the tax.

How to make the choice. Make the choice by attaching a filled-in Form 2119, *Sale of Your Home*, to your income tax return for the year in which you sell your home. However, if you do not have Form 2119, you can make the choice by attaching a signed statement to your return. The statement must say you choose to exclude from income the gain from the sale. It must also include:

- 1) Your name, age, social security number, and marital status on the date of the sale. If jointly owned, give this information for each owner.
- 2) The dates you bought and sold the home.
- 3) The amount realized and the adjusted basis of the property on the date of sale.
- 4) How long you were away from the home during the 5 years before the sale. Do not include vacation and other seasonal absences, even if you rented out the home during those absences.
- 5) Whether you or a joint owner ever chose to exclude gain on the sale of a home, and if you did, when and where you did so. If you revoked the choice, give the date you revoked it.

You can choose to exclude the gain even if you originally included it on your tax return for the year of the sale. You do so by filing an amended return (Form 1040X) for that year. You must send a filled-in Form 2119 or a statement that includes the information listed above with your amended return. See *How to revoke the choice*, later.

Example 1. Tom White, a single person, sold his main home on September 15, 1994. Tom was 58 years old when he sold the house and had owned and lived in the property as his main home for the past 10 years. He has never excluded gain on the sale of a home. This year he chooses to exclude the gain on the sale of his home. Tom's Form 2119 appears later in this publication.

Tom figures the gain on the sale of his home in the following way:

a) Selling price of home	\$130,000
b) Minus: Selling expenses	10,000
c) Amount realized on sale	\$120,000
d) Minus: Adjusted basis of old home (original cost plus improvements)	50,000
e) Gain realized	<u>\$ 70,000</u>

Because Tom is not planning to replace his home, he does not complete all of Part III of Form 2119. He completes lines 1 through 15 and attaches it to his tax return.

Example 2. Edward and Elizabeth Jones sold their home on June 15, 1994, for \$250,000. Both are 60 years old and had owned and lived in the home as their main home for 20 years. The adjusted basis of the old home was \$75,000 and they had selling expenses of \$15,000. They bought a new home for \$110,000 and moved into it on July 20, 1994. Neither spouse has excluded gain on the sale of a home before, and they choose to exclude \$125,000 of the gain on the sale of their old home in 1994.

They must postpone the part of the gain not excluded. This is because they purchased a new home that cost as much as the adjusted sales price of the old home. The Joneses' Form 2119 appears later in this publication.

The Joneses figure the gain excluded and postponed as follows:

<u>Gain Realized</u>	
a) Selling price of old home	\$250,000
b) Minus: Selling expenses	15,000
c) Amount realized on sale	\$235,000
d) Minus: Adjusted basis of old home	75,000
e) Gain realized	<u>\$160,000</u>

<u>Gain after Exclusion</u>	
f) Gain realized [line (e)]	\$160,000
g) Minus: Exclusion [smaller of (e) or \$125,000]	125,000
h) Gain after exclusion	<u>\$ 35,000</u>

<u>Gain Taxed in 1994</u>	
i) Amount realized [line (c)]	\$235,000
j) Minus: Exclusion [line (g)]	125,000
k) Adjusted sales price	\$110,000
l) Minus: Cost of new home	110,000
m) Gain taxed in 1994	<u>\$ -0-</u>

<u>Gain Postponed</u>	
n) Gain after exclusion [line (h)]	\$ 35,000
o) Minus: Gain taxed in 1994 [line (m)]	-0-
p) Gain postponed	<u>\$ 35,000</u>

<u>Adjusted Basis of New Home</u>	
q) Cost of new home [line (l)]	\$110,000
r) Minus: Gain postponed [line (p)]	35,000
s) Adjusted basis of new home	<u>\$ 75,000</u>

How to revoke the choice. You can revoke your choice to exclude gain by filing an amended return for the year of sale using Form 1040X. Attach a new completed Form

2119 and, if needed, a Schedule D (Form 1040). Send the forms to the Internal Revenue Service Center for the place where you live.

If you were married when you sold your home, your spouse who joined you in making the choice must join you in revoking it. If your spouse is deceased, his or her personal representative must join you in revoking the choice.

Example. On October 2, Joe Brown sold his separately owned home. Two months later his wife Joyce died, leaving a will that appointed the First National Bank of Hometown

as her executor. When preparing his tax return in March, Joe had the bank join him in making the choice. If later he wants to revoke the choice, the bank must join him in revoking it.

Note. If you revoke your choice to exclude gain when less than a year is left in the assessment period (time for determining your correct tax) for the return on which the choice was made, you must agree to extend the assessment period. Before the end of the period, you

must file a statement that the assessment period will not end until 1 year after the date the statement is filed. The assessment period normally ends on the latest of the dates shown earlier under *Time to exclude gain*.

Form 2119 - Harris
Form 2119 - White
Form 2119 - Jones

Sale of Your Home

Department of the Treasury
Internal Revenue Service

▶ Attach to Form 1040 for year of sale.

▶ See separate instructions. ▶ Please print or type.

Your first name and initial. If a joint return, also give spouse's name and initial. FRANK G. and EVELYN M. HARRIS		Last name HARRIS	Your social security number 222 : 00 : 2222
Fill in Your Address Only If You Are Filing This Form by Itself and Not With Your Tax Return	Present address (no., street, and apt. no., rural route, or P.O. box no. if mail is not delivered to street address) 2161 CITATION DRIVE	Spouse's social security number 444 : 00 : 4444	
	City, town or post office, state, and ZIP code ANYTOWN, MD 21000		

Part I Gain on Sale

1	Date your former main home was sold (month, day, year)	▶	1	5 / 6 / 94
2	Have you bought or built a new main home?			<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
3	If any part of either main home was ever rented out or used for business, check here ▶ <input type="checkbox"/> and see instructions.			
4	Selling price of home. Do not include personal property items you sold with your home		4	87,000
5	Expense of sale (see instructions)		5	5,200
6	Subtract line 5 from line 4		6	81,800
7	Adjusted basis of home sold (see instructions)		7	63,000
8	Gain on sale. Subtract line 7 from line 6		8	18,800

Is line 8 more than zero?

Yes → If line 2 is "Yes," you must go to Part II or Part III, whichever applies. If line 2 is "No," go to line 9.
No → Stop and attach this form to your return.

9 If you haven't replaced your home, do you plan to do so within the replacement period (see instructions)? Yes No
• If line 9 is "Yes," stop here, attach this form to your return, and see **Additional Filing Requirements** in the instructions.
• If line 9 is "No," you must go to Part II or Part III, whichever applies.

Part II One-Time Exclusion of Gain for People Age 55 or Older—By completing this part, you are electing to take the one-time exclusion (see instructions). If you are not electing to take the exclusion, go to Part III now.

10	Who was age 55 or older on the date of sale?	<input type="checkbox"/> You <input type="checkbox"/> Your spouse <input type="checkbox"/> Both of you
11	Did the person who was age 55 or older own and use the property as his or her main home for a total of at least 3 years (except for short absences) of the 5-year period before the sale? If "No," go to Part III now	<input type="checkbox"/> Yes <input type="checkbox"/> No
12	At the time of sale, who owned the home?	<input type="checkbox"/> You <input type="checkbox"/> Your spouse <input type="checkbox"/> Both of you
13	Social security number of spouse at the time of sale if you had a different spouse from the one above. If you were not married at the time of sale, enter "None"	▶
14	Exclusion. Enter the smaller of line 8 or \$125,000 (\$62,500 if married filing separate return). Then, go to line 15	14

Part III Adjusted Sales Price, Taxable Gain, and Adjusted Basis of New Home

15	If line 14 is blank, enter the amount from line 8. Otherwise, subtract line 14 from line 8 • If line 15 is zero, stop and attach this form to your return. • If line 15 is more than zero and line 2 is "Yes," go to line 16 now. • If you are reporting this sale on the installment method, stop and see the instructions. • All others, stop and enter the amount from line 15 on Schedule D, col. (g), line 4 or line 12.	15	18,800
16	Fixing-up expenses (see instructions for time limits)	16	500
17	If line 14 is blank, enter amount from line 16. Otherwise, add lines 14 and 16	17	500
18	Adjusted sales price. Subtract line 17 from line 6	18	81,300
19a	Date you moved into new home ▶ 5 / 4 / 94 b Cost of new home (see instructions)	19b	77,200
20	Subtract line 19b from line 18. If zero or less, enter -0-	20	4,100
21	Taxable gain. Enter the smaller of line 15 or line 20 • If line 21 is zero, go to line 22 and attach this form to your return. • If you are reporting this sale on the installment method, see the line 15 instructions and go to line 22. • All others, enter the amount from line 21 on Schedule D, col. (g), line 4 or line 12, and go to line 22.	21	4,100
22	Postponed gain. Subtract line 21 from line 15	22	14,700
23	Adjusted basis of new home. Subtract line 22 from line 19b	23	62,500

Sign Here Only If You Are Filing This Form by Itself and Not With Your Tax Return	Under penalties of perjury, I declare that I have examined this form, including attachments, and to the best of my knowledge and belief, it is true, correct, and complete.			
	Your signature	Date	Spouse's signature	Date
	If a joint return, both must sign.			

Sale of Your Home

Department of the Treasury
Internal Revenue Service

▶ Attach to Form 1040 for year of sale.

▶ See separate instructions. ▶ Please print or type.

Your first name and initial. If a joint return, also give spouse's name and initial.		Last name		Your social security number	
TOM S. WHITE		WHITE		333 00 3333	
Fill in Your Address Only if You Are Filing This Form by Itself and Not With Your Tax Return	Present address (no., street, and apt. no., rural route, or P.O. box no. If mail is not delivered to street address)			Spouse's social security number	
	2331 MINTON LANE				
City, town or post office, state, and ZIP code					
ANYTOWN, NY 10000					

Part I Gain on Sale

1	Date your former main home was sold (month, day, year)	▶	1	9	15	194
2	Have you bought or built a new main home?		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No			
3	If any part of either main home was ever rented out or used for business, check here ▶	<input type="checkbox"/>	and see instructions.			
4	Selling price of home. Do not include personal property items you sold with your home		4	130,000		
5	Expense of sale (see instructions)		5	10,000		
6	Subtract line 5 from line 4		6	120,000		
7	Adjusted basis of home sold (see instructions)		7	50,000		
8	Gain on sale. Subtract line 7 from line 6		8	70,000		

Is line 8 more than zero?

Yes → If line 2 is "Yes," you must go to Part II or Part III, whichever applies. If line 2 is "No," go to line 9.
No → Stop and attach this form to your return.

- 9 If you haven't replaced your home, do you plan to do so within the replacement period (see instructions)? Yes No
 • If line 9 is "Yes," stop here, attach this form to your return, and see **Additional Filing Requirements** in the instructions.
 • If line 9 is "No," you must go to Part II or Part III, whichever applies.

Part II One-Time Exclusion of Gain for People Age 55 or Older—By completing this part, you are electing to take the one-time exclusion (see instructions). If you are not electing to take the exclusion, go to Part III now.

10	Who was age 55 or older on the date of sale?	<input checked="" type="checkbox"/> You	<input type="checkbox"/> Your spouse	<input type="checkbox"/> Both of you
11	Did the person who was age 55 or older own and use the property as his or her main home for a total of at least 3 years (except for short absences) of the 5-year period before the sale? If "No," go to Part III now	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No	
12	At the time of sale, who owned the home?	<input checked="" type="checkbox"/> You	<input type="checkbox"/> Your spouse	<input type="checkbox"/> Both of you
13	Social security number of spouse at the time of sale if you had a different spouse from the one above. If you were not married at the time of sale, enter "None"	▶		
13		NONE		
14	Exclusion. Enter the smaller of line 8 or \$125,000 (\$62,500 if married filing separate return). Then, go to line 15	▶		
14		70,000		

Part III Adjusted Sales Price, Taxable Gain, and Adjusted Basis of New Home

15	If line 14 is blank, enter the amount from line 8. Otherwise, subtract line 14 from line 8	15	-0-
• If line 15 is zero, stop and attach this form to your return. • If line 15 is more than zero and line 2 is "Yes," go to line 16 now. • If you are reporting this sale on the installment method, stop and see the instructions. • All others, stop and enter the amount from line 15 on Schedule D, col. (g), line 4 or line 12.			
16	Fixing-up expenses (see instructions for time limits)	16	
17	If line 14 is blank, enter amount from line 16. Otherwise, add lines 14 and 16	17	
18	Adjusted sales price. Subtract line 17 from line 6	18	
19a	Date you moved into new home ▶	19b	Cost of new home (see instructions)
20	Subtract line 19b from line 18. If zero or less, enter -0-	20	
21	Taxable gain. Enter the smaller of line 15 or line 20	21	
• If line 21 is zero, go to line 22 and attach this form to your return. • If you are reporting this sale on the installment method, see the line 15 instructions and go to line 22. • All others, enter the amount from line 21 on Schedule D, col. (g), line 4 or line 12, and go to line 22.			
22	Postponed gain. Subtract line 21 from line 15	22	
23	Adjusted basis of new home. Subtract line 22 from line 19b	23	

Under penalties of perjury, I declare that I have examined this form, including attachments, and to the best of my knowledge and belief, it is true, correct, and complete.

Sign Here Only if You Are Filing This Form by Itself and Not With Your Tax Return	Your signature	Date	Spouse's signature	Date
	If a joint return, both must sign.			

Sale of Your Home

1994

Attachment Sequence No. 20

Department of the Treasury
Internal Revenue Service

▶ Attach to Form 1040 for year of sale.

▶ See separate instructions. ▶ Please print or type.

Your first name and initial. If a joint return, also give spouse's name and initial. EDWARD and ELIZABETH M. JONES		Last name JONES	Your social security number 555:00:5555
Fill in Your Address Only If You Are Filing This Form by Itself and Not With Your Tax Return	Present address (no., street, and apt. no., rural route, or P.O. box no. if mail is not delivered to street address) 4238 COTTAGE COURT		Spouse's social security number 777:00:7777
	City, town or post office, state, and ZIP code ANYTOWN, AZ 86000		

Part I Gain on Sale

1	Date your former main home was sold (month, day, year)	▶	1 6 15 194
2	Have you bought or built a new main home?		<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
3	If any part of either main home was ever rented out or used for business, check here ▶	<input type="checkbox"/>	and see instructions.
4	Selling price of home. Do not include personal property items you sold with your home		4 250,000
5	Expense of sale (see instructions)		5 15,000
6	Subtract line 5 from line 4		6 235,000
7	Adjusted basis of home sold (see instructions)		7 75,000
8	Gain on sale. Subtract line 7 from line 6		8 160,000

Is line 8 more than zero?	Yes	→	If line 2 is "Yes," you must go to Part II or Part III, whichever applies. If line 2 is "No," go to line 9.
	No	→	Stop and attach this form to your return.

- 9 If you haven't replaced your home, do you plan to do so within the replacement period (see instructions)? Yes No
- If line 9 is "Yes," stop here, attach this form to your return, and see **Additional Filing Requirements** in the instructions.
 - If line 9 is "No," you must go to Part II or Part III, whichever applies.

Part II One-Time Exclusion of Gain for People Age 55 or Older—By completing this part, you are electing to take the one-time exclusion (see instructions). If you are not electing to take the exclusion, go to Part III now.

10	Who was age 55 or older on the date of sale?	<input type="checkbox"/> You <input type="checkbox"/> Your spouse <input checked="" type="checkbox"/> Both of you
11	Did the person who was age 55 or older own and use the property as his or her main home for a total of at least 3 years (except for short absences) of the 5-year period before the sale? If "No," go to Part III now	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
12	At the time of sale, who owned the home?	<input type="checkbox"/> You <input type="checkbox"/> Your spouse <input checked="" type="checkbox"/> Both of you
13	Social security number of spouse at the time of sale if you had a different spouse from the one above. If you were not married at the time of sale, enter "None"	▶
14	Exclusion. Enter the smaller of line 8 or \$125,000 (\$62,500 if married filing separate return). Then, go to line 15	
		14 125,000

Part III Adjusted Sales Price, Taxable Gain, and Adjusted Basis of New Home

15	If line 14 is blank, enter the amount from line 8. Otherwise, subtract line 14 from line 8		15 25,000
	• If line 15 is zero, stop and attach this form to your return.		
	• If line 15 is more than zero and line 2 is "Yes," go to line 16 now.		
	• If you are reporting this sale on the installment method, stop and see the instructions.		
	• All others, stop and enter the amount from line 15 on Schedule D, col. (g), line 4 or line 12.		
16	Fixing-up expenses (see instructions for time limits)		16 -0-
17	If line 14 is blank, enter amount from line 16. Otherwise, add lines 14 and 16		17 125,000
18	Adjusted sales price. Subtract line 17 from line 6		18 110,000
19a	Date you moved into new home ▶ 7 20 194	b Cost of new home (see instructions)	19b 110,000
20	Subtract line 19b from line 18. If zero or less, enter -0-		20 -0-
21	Taxable gain. Enter the smaller of line 15 or line 20		21 -0-
	• If line 21 is zero, go to line 22 and attach this form to your return.		
	• If you are reporting this sale on the installment method, see the line 15 instructions and go to line 22.		
	• All others, enter the amount from line 21 on Schedule D, col. (g), line 4 or line 12, and go to line 22.		
22	Postponed gain. Subtract line 21 from line 15		22 55,000
23	Adjusted basis of new home. Subtract line 22 from line 19b		23 75,000

Sign Here Only If You Are Filing This Form by Itself and Not With Your Tax Return	Under penalties of perjury, I declare that I have examined this form, including attachments, and to the best of my knowledge and belief, it is true, correct, and complete.			
	Your signature	Date	Spouse's signature	Date
	If a joint return, both must sign.			

Glossary

The definitions in this glossary are the meanings of the terms as used in this publication. The same term used in another publication may have a slightly different meaning.

Note: Certain definitions show words in ***bold italicized*** print. This means that those words are also defined in this glossary.

Adjusted basis: This is your ***basis*** in the property increased or decreased by certain amounts. See *Adjusted Basis*, earlier in this publication, for a list of amounts that increase or decrease your basis in the property.

Adjusted sales price: This is the ***amount realized*** minus any ***one-time exclusion*** you claim on your Form 2119 and minus any ***fixing-up expenses*** you might have.

Amount realized: This is the selling price of your old home minus your ***selling expenses***.

Basis: Your basis in the property is determined by how you got it. If you bought or built the property, your basis is what it cost you. If you got the property in some other way, your basis will be determined differently. See *Cost As Basis* and *Other Basis* earlier in this publication for more information.

Date of sale: If you received a Form 1099-S, *Proceeds From Real Estate Transactions*, the date should be shown in box 1. If you did not receive this form, the date of sale is the earlier of (a) the date title transferred or (b) the date the economic burdens and benefits of ownership shifted to the buyer. In most cases, these dates are the same.

Fixing-up expenses: These are costs you pay for decorating or repairing your home to make it easier to sell. You may be able to deduct fixing-up expenses from the ***amount realized*** on the sale of your old home. See *Fixing-up expenses*, earlier in this publication, to

determine how you treat these expenses when you sell your old home.

Gain: Your gain on the sale of your home is the ***amount realized*** minus the ***adjusted basis*** of the home you sold.

Improvements: These are costs that add to the value of your home, prolong the life of the property, or allow the property to be used for new purposes. The cost of improvements increases your ***basis*** in the property. See *Table 1, Examples of Improvements*, earlier in this publication.

Main home: This is the home you live in most of the time. It can be a house, houseboat, cooperative apartment, condominium, etc. You must have a legal interest in the home (i.e., legal title) for it to be your main home.

One-time exclusion: This is a once-in-a-lifetime election available to persons age 55 or older to exclude up to \$125,000 of the ***gain*** from the sale of a ***main home***. Generally the person is required to have owned and lived in the home for at least 3 years during a 5-year period ending on the ***date of sale***. The excluded gain is never taxed. For more details, see *Exclusion of Gain*, earlier in this publication.

Postponement of gain: If you sell your ***main home***, and buy and live in a new main home within a certain ***replacement period***, some or all of any gain on the sale will not be taxed in the year of sale if the cost of the new home is the same as or more than the ***adjusted sales price*** of the old home. Instead, the gain not taxed in the year of sale reduces your ***basis*** in the new home that you purchase. If you sell the new home in a later year and again replace

it, you continue to postpone tax on your gain. For a detailed discussion, see *Postponement of Gain* earlier in this publication.

Repairs: These are costs that maintain your property in good condition. These costs differ from ***improvements*** in that they do not add much to the value or life of the property and do not increase your ***basis*** in the property.

Replacement period: This is the period you have to replace your old ***main home*** with a new one for purposes of ***postponement of gain***. Generally you have 2 years before or 2 years after the ***date of sale*** of your old home to replace it. See *Time Allowed for Replacement* earlier in this publication for exceptions to the above rule which may give you a longer replacement period.

Seller-financed mortgage: This is a mortgage that you give to the buyer of your home. The buyer makes mortgage payments to you.

Selling expenses: Selling expenses include items such as sales commissions, and advertising and legal fees you pay to sell your home. Selling expenses also usually include loan charges you pay in selling your home, such as loan placement fees or "points."

Settlement fees (or closing costs): These are amounts paid in purchasing your property in addition to the contract price. Some of these amounts are added to the ***basis*** of the property and some are deductible as itemized deductions. Certain amounts are neither deductible or added to the basis of the property. See *Settlement fees or closing costs* earlier in this publication for more details.

