Capital Gains Taxes

Almost everything you own and use for personal purposes, pleasure or investment is a capital asset. Your main home or investment property is no exception. When you sell a capital asset, such as your home, the difference between the amount you sell it for and your basis, which is usually what you paid for it, is capital gains or capital loss. While you must report all capital gains, you may deduct only your capital losses on investment property, not personal property.

What are short-term vs. long-term capital gains and losses? Capital gains and losses are classified as long-term or short-term, depending on how long you hold the property before you sell it. If you hold it more than one year, your capital gains or loss is long-term. If you hold it one year or less, your capital gains or loss is short-term.

What is the basis and how is it determined? You need to know your basis in your home to calculate any gain or loss when you sell it. Your basis is determined by how you acquired your home. If you purchased or built it, your basis is your initial cost. If you acquired it in some other way (inheritance, gift, etc), you must know its adjusted basis to the donor just before it was given to you. You also must know its fair market value (FMV) at the time title was transferred. For more information, log onto www.irs.gov and search for publication 551 (Basis of Assets).

What are the current capital gains rates? Generally, for most taxpayers, net capital gain is taxed at rates no higher than 15%. Some or all net capital gain may be taxed at 0% if you are in the 10% to 15% ordinary income tax brackets. However, beginning in 2013, a new 20% rate on net capital gain applies to the extent that a taxpayer's taxable income exceeds the thresholds set for the new 39.6% ordinary tax rate ($400,000 for single; $450,000 for married filing jointly or qualifying widow(er); $425,000 for head of household, and $225,000 for married filing separately). Publication 505

If I make a profit from selling my home, do I get to keep any of it tax-free? As a single homeowner, you can exclude up to $250,000 of capital gains. If you are married filing separately, each of you can exclude up to $250,000. If you are married filing jointly, together you can exclude up to $500,000 of capital gains.

Is this a one-time exclusion? The exclusion is allowed each time you sell or exchange your principal residence, as often as every two years. And you are not required to reinvest your proceeds in a new residence to claim the exclusion.

What is the ownership and usage criteria for claiming the exclusion? To be eligible, you must have owned and lived in your home as your primary residence for a combined period of at least two of the last five years prior to selling or exchanging your principal residence. What is a real estate depreciation recapture? Depreciation is the decrease in the value of property over the time the property is used. Depreciation recapture is when a property used for business purposes is sold at a gain; if accelerated depreciation has been claimed, you may be required to pay tax at ordinary income rates to the extent of the excess accelerated depreciation.

We own rental property. If we live in it as our main home for two years, can we sell it and not pay capital gains tax?
You may be able to exclude your allowed amount of capital gains from the sale of your main home that you have also used for business or rental property if you meet the ownership and use criteria outlined in the above paragraph. However, if you took depreciation on your home used for business or rental property, you cannot exclude the part of your gain equal to the depreciation taken or allowable for the periods after May 1997. If you can prove that the depreciation taken was less than the amount allowable, the amount you cannot exclude is the lesser of the two figures. Refer to publication 523 on www.irs.gov for more information.

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