



TRICKS OF THE TRADE

TAKING A TAX LOSS ON THE SALE OF YOUR PRIMARY RESIDENCE

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Let's begin by noting that the IRS laws do not allow you to take a loss on the sale of your primary residence. So, how can you do it?

I recently had a client who was retiring and moving to another state, and planned to sell her home. She had already considered getting an apartment so that she could show her home without having to take her pets to the kennel when prospects came for showings. This is what prompted my idea of selling her primary residence at a loss, so we called our CPA to confirm we could implement my idea, but within the confines of the IRS rules.

A taxpayer may NOT take a tax loss on the sale of their primary residence, but they CAN take a loss on the sale of a rental property. Thus, in November 2018, the client decided to convert her primary residence to a rental property. She got an appraisal for the home, which was now considered to be her cost basis for her home. She rented her home for about 6 months, crossing over calendar years. She subsequently sold her house in May 2019 and was able to take the loss.

In her particular instance, it was an enormous windfall. She was able to have the house appraised for \$675,000, despite only selling it for about \$530,000. This gave her a \$145,000 capital loss, the rental "loss" for those 6 months, AND the reduction in sale price for the realtor fee. In the end, there was a roughly \$175,000 loss she took on the property.

It gets better! Unlike capital losses from investments that are limited to \$3,000 on your tax return, she was able to take the entire \$175,000 loss directly against her ordinary income. This loss can provide many favorable results. In her case, that loss offset a \$175,000 conversion from her IRA into a Roth IRA and effectively paying no income tax on the conversion. This was a HUGE win, to the tune of a tax savings of almost \$50,000, which was far greater than the cost of renting an apartment for 6 months.

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Note that this strategy can also be applied to a vacation home, as vacation homes are treated like primary residences as they pertain to claiming losses when sold. If any of these situations may apply to you, contact your financial advisor, and also confirm with your CPA or tax preparer to review the specific tax laws as they may pertain to your situation.

Look for next month's "Trick of the Trade" on ways to reduce or eliminate a capital gain from the sale of your vacation home!