



Jill B. Boynton, CFP®, CDFA
Cornerstone Financial Planning, LLC
(603) 431-1133

jill@cornerstoneplanning.com
www.cornerstoneplanning.com
70 Old Post Road
Newington, NH 03801

Divorce Advisor

Financial advice for family law

June 2013

Selling Rental Properties

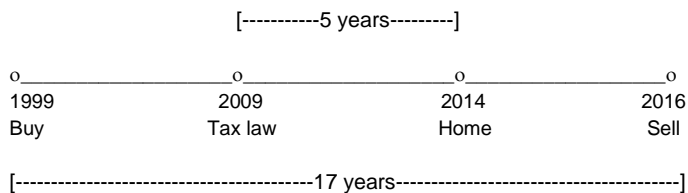
Sometimes in a divorce one spouse will move into a second home that the couple had owned while married. Often the property had been rented and the spouse receiving the property decides to convert it to their personal residence. When the property is sold in the future some of the gain might be taxable due to a tax law effective January 1, 2009 concerning the conversion of a rental property into a primary residence.

Before this tax law passed, if someone moved into a rental, lived in it for a minimum of two years, and then sold it, they could apply their entire \$250,000 exclusion toward the capital gain. By living in it for 2 of the 5 years before it was sold they had effectively converted it back to a personal residence.

But let's look at the effect of the current tax law:

Example #1: Karen and Derek bought a rental property in 1999. Now it is 2009 and they are getting divorced. The rental property has grown in value. Karen receives the rental as part of her property settlement. She keeps it as a rental for another 5 years until 2014.

Karen moves into the rental in 2014 and lives there for 2 years before selling it in 2016. By the time she sells it she has owned it for 17 years. Of those 17 years, it was a rental property for five years after January 1, 2009.



To figure how much gain she is taxed on, take the total number of years it was a rental after 1/1/09 (5) divided by the total numbers of years owned (17).

She is taxed on 5/17ths of the gain (after **taxing all of the allowed depreciation as a rental property**). The remaining 12/17ths can be offset by the \$250,000 exclusion.

Note that the IRS will tax Karen on all of the depreciation she was allowed to take, even if she didn't take it on her past tax returns!

Example #2: Assume Karen moved into the rental in 2006. She lived there for 3 years and sold it on January 1, 2009. How much gain is she taxed on?

She can exclude as much as \$250,000 because it was not a rental after 1/1/09 and the new tax law had not gone into effect yet. However, she will always pay tax on the gain equal to the depreciation taken while the property was rented, even if the total gain is less than \$250,000.

Our examples are of a couple getting divorced. However, this tax law applies to anyone who turns a rental property into a primary residence.

Copyright © Financial Divorce Association, Inc.

Jill B. Boynton, CFP®,
Certified Financial
Divorce Analyst, has
been assisting clients
going through divorce
since 2004. She has
helped attorneys and
their clients work
through the financial
aspects of divorce,
bringing clarity and
fairness to the process.

