

Washington Report: Capital Gains Takes on Change

by *Kenneth R. Harney*

Hardly anybody noticed it, but Congress tucked away a valuable bit of holiday cheer for real estate when it passed its final tax bill of the year.

It was the first substantive change in years to the generous capital gains rules governing sales of principal homes.

Most homeowners and real estate professionals can recite these rules in their sleep: Married, joint-filing sellers of houses can exclude up to \$500,000 of gain, and single-filing sellers can take up to \$250,000 ... provided they've used the property as a principal residence for a cumulative two of the previous five years.

But what happens when a married home owner dies? Does the surviving spouse still qualify for the full \$500,000 -- or does she or he only get to exclude \$250,000?

The answer from the IRS has been this: you only get the full \$500,000 if you sell during the tax year in which you were married and filing a joint return. Otherwise, the tax code sees you as single, and then you're limited to \$250,000.

In other words, if your wife or husband died in June of 2007, you can only claim the full \$500,000 benefit if you sell before December 31, 2007.

After that, as long as you remain unmarried, you're capped at the \$250,000 limit for single taxpayers.

As a practical matter, most surviving spouses inherit their husband's or wife's share of the property at what's known as a "stepped up" tax basis, with no capital gains tax liability at the current market value.

But here's the problem: Some surviving spouses complain that they feel rushed into sales by the current tax rules. This is especially true for people who've lost their loved ones during the final few months of the year.

With everything else going on, they don't want the additional pressure of having to make the decision to sell the family home quickly. They want more time. Fair enough.

Well, now they've got it. Legislation signed into law before the holiday recess gives surviving spouses two full years to qualify for the \$500,000 exclusion -- even though technically they're single.

And who says Congress doesn't have a heart?

Since your tax professional may not be familiar with this yet, here's the official citation: The bill is H.R.3648. The capital gains change is in Section 7.

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