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How to Keep More of Your Home-Sale Capital Gains

COUNTING HOUSE |

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Having a proper plan in place before selling can help you reduce your tax bill.

With American households sitting on \$34.5 trillion in home equity in the first quarter of 2025, according to online loan marketplace LendingTree, a lot of cash will be unlocked when these homes sell. Many of those sellers will face looming capital-gains tax bills. The good news: With proper tax planning upfront, it is possible to minimize those taxes or eliminate them altogether.

Karla Dennis, an enrolled tax agent and the chief executive officer of KDA, a tax-strategy firm in La Palma, Calif., said that one of the most common ways homeowners can reduce taxes on the sale of their primary residence is the exclusion authorized by the Internal Revenue Code. It allows single taxpayers to exclude \$250,000 of gain and married taxpayers who file jointly to exclude \$500,000. Surviving spouses can still take the entire \$500,000 exclusion as long as they sell the home within two years of the death of their spouse. *Note*

There are a few key points to remember: These exclusions only apply to the sale of a primary residence and you must have owned the property as your primary home for two years out of the five years leading up to the sale. You also cannot take the exclusion if you already excluded the gain from the sale of another home within the prior two years.

But even these exclusions may not be sufficient to help sellers avoid taxes. According to the National Association of Realtors, 34% of homeowners today could already exceed the \$250,000 capital gains exclusion cap for single filers, while 10% have potential gains above the \$500,000 threshold for married couples filing jointly.

Note
You must own a home for at least a year to qualify for longterm capital gains rates. Shortterm gains are taxed at ordinary income rates on the federal level.

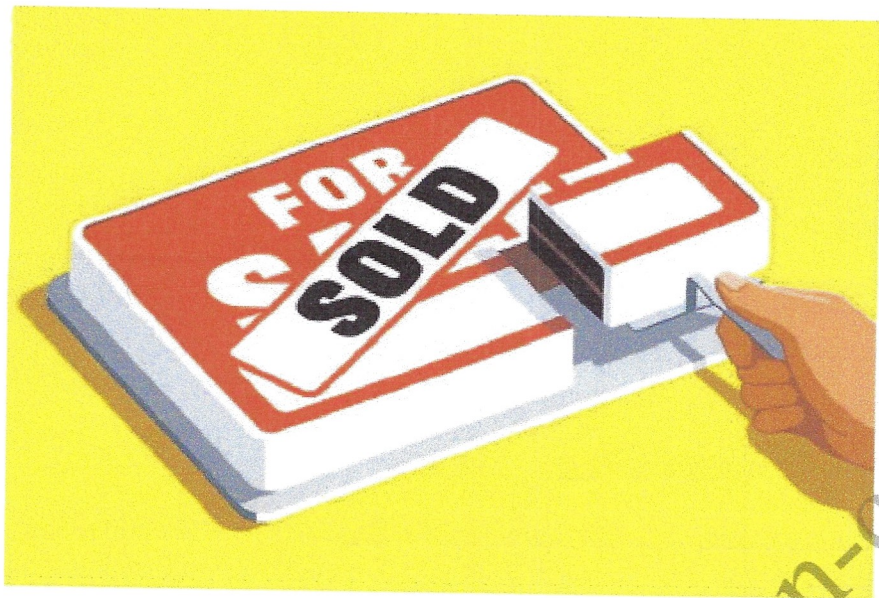
There are also state capital gains taxes to consider. While no capital-gains taxes would be due in states such as Florida, which have no state income tax, sellers in other states will pay dearly. In New York state, for example, where long-term capital gains are taxed at ordinary income rates, sellers could pay up to 10.9%, depending on their income level.

Note
The death of a homeowner can eliminate capital gains, though the owner obviously won't be around to benefit. After a homeowner's death, the home's basis (the original acquisition price plus capitalized improvement costs) is set to the market value on the date of the owner's death. If heirs sell it for that price, there would be no capital gain, thus no tax due. *Note*

Those who can't avoid capital gains taxes should consider taxloss harvesting, or offsetting capital gains with tax losses, which can reduce the overall taxes due. If you have investment losses on stocks, bonds or mutual funds that you may not recoup in the short term, for example, consider selling them to offset the gains.

If you're getting ready to sell your primary residence, here are some additional things to consider.

Search for receipts. The adjusted basis of



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your home is generally calculated by adding the cost of capital improvements to the price you paid to acquire your home. So, if you replaced your roof or remodeled your kitchen, those costs should be added to the price you paid for the house, as are fees and closing costs, such as title insurance and recording fees. The adjusted basis is deducted from the amount realized from the sale to arrive at the taxable gain or loss, so the more capital improvements you completed, the lower the ultimate gain.

The practical problem is that most home sellers don't have good records and, after what may be decades of ownership, they can't substantiate the cost of capital improvements.

"Keeping track of capital improvements for the IRS is a challenge because a lot of people just don't think about it," said Rob Wall, a tax partner at law firm Akerman LLP in Winston-Salem, N.C. "If somebody is preparing to sell their house, they need to do a historic search of their own records to see what they've done to improve the house."

Jacob Wood, an associate real estate broker with Coldwell Banker Warburg in Brooklyn, N.Y., sold an Upper West Side duplex in 2022 where the seller had previously spent \$85,000 to renovate a bathroom and add a bedroom. Because she was able to document the expenditure, she saved \$16,000 in capital-gains taxes she otherwise would have had to pay. "She had an itemized sheet for the project," Wood said. "Not only did she still have the records, but the general contractor was still in business and could get her any documentation she needed."

Finance the sale. If you don't need the equity from your home to purchase another one, consider financing the purchase for your buyer, using an installment sale. Gains on installment sales are recognized as capital gains, while interest is taxed as ordinary income, as each payment is received, allowing you to spread out the gain—and taxes due—over the life of the mortgage. Structuring the deal as an installment sale could also prevent you from being bumped into a higher tax bracket for the year of the sale, which could happen if the entire gain were included in your income in that year, Wall said. The risk of this strategy is that the buyer could default on the loan.

Convert your home to business property. If you rent your house rather than sell it, you will be converting it to business property. That way, you can later dispose of the property via a 1031 "like-kind" exchange, which allows you to defer the gain, rather than pay taxes immediately. Ultimately, when you sell the replacement property, you'll be liable for capital-gains taxes then—unless you pass away, which allows your heirs to inherit the property at a stepped-up basis with no taxes due.