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Vacation & 2nd Homes Qualify for Tax Deferral

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Owners enjoy many of the "home away from home" comforts in their vacation property, but when it comes time to sell, they do not benefit from the same tax exclusions as that of a primary residence sale. Capital gains and possibly recapture taxes apply. Furthermore, a second home with strictly personal use will not qualify for a tax deferral: the reasoning that "holding this property with the hope of future gain" is not enough to qualify the property as "held for investment" under the IRC §1031 Tax Code.

Thus, questions remain: In order to defer the tax, how long do I have to rent out the property and how much can I use it? The IRS provided these answers in Rev. Proc. 2008-16: for a "dwelling unit" to qualify as property held for investment purposes and eligible for 1031 Exchange treatment, the Taxpayer must have:

- 1) owned it for 24 months immediately before the sale/exchange, and
- 2) rented it at fair market rental for fourteen days or more within each of the past two 12-month periods the Exchanger, and
- 3) restricted his/her personal use to not exceed the greater of 14 days or 10% of the total number of days that it was rented within each of those 12-month periods.

The replacement property must meet the same criteria as noted above, and the exchange itself must meet all other §1031 requirements.

Planning ahead is crucial - converting a personal use property to a qualified rental now can develop into a great tax savings benefit in the not-so-distant future!

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