

## PERSONAL RESIDENCE: ANNUAL DEDUCTIONS

- **Mortgage interest:** Deductible on your primary residence if you itemize—subject to limits based on when the mortgage originated
- **Property taxes:** Fall under the SALT (State and Local Tax) cap along with state income taxes and DMV fees
- **Itemizing requirement:** Your combined itemized deductions must exceed the standard deduction to benefit

## TAX BASIS IN YOUR HOME

- Your tax basis starts with what you paid for the property, regardless of your down payment or mortgage amount
- **Home improvements** (new rooms, pools, major repairs) increase your basis—reducing potential taxable gain when you sell
- **Keep your receipts:** Documentation of improvements can save you significantly when it comes time to sell

## CAPITAL GAINS EXCLUSION (SECTION 121)

- If you've lived in your home as a primary residence for at least **2 of the last 5 years**, you may exclude gain when you sell
- Exclusion amounts vary based on filing status
- Both spouses must meet the residency requirement to qualify for the higher married exclusion
- **Planning tip:** If you've owned your home for many years, consider how much gain you may be sitting on before deciding to sell

## RENTAL PROPERTY: DEPRECIATION BASICS

- Unlike personal residences, rental properties allow you to deduct **depreciation** on the building (not land)
- **Building vs. land allocation:** How value is split between building and land matters—you can only depreciate the building portion
- Property tax statements and appraisals can help support your allocation, but documentation is key

## REAL ESTATE PROFESSIONAL STATUS

- Qualifying as a real estate professional allows rental losses to offset other income—but there's a **high bar** to meet
- Requires significant time spent on real estate activities, and it must represent the majority of your earnings
- **Common scenario:** One spouse works full-time while the other manages the real estate portfolio and qualifies for this status
- Additional benefits include the ability to make retirement contributions based on real estate income
- This is not something to claim lightly—proper documentation and consistency are essential

## ESSENTIAL TAKEAWAYS

- ✓ **Keep records** of all home improvements—they increase your tax basis
- ✓ The **Section 121 exclusion** can eliminate tax on home sale gains if you meet residency requirements
- ✓ Rental properties offer **depreciation deductions** not available for personal residences
- ✓ **Real estate professional** status has significant benefits but requires meeting strict requirements
- ✓ The **passive loss exception** may help if you're actively involved and meet income thresholds
- ✓ **Cost segregation** can accelerate deductions but is typically worthwhile only for higher-value properties
- ✓ The **QBI deduction** is frequently overlooked—ask your CPA if you qualify

**Action Item:** Review your real estate holdings with your tax professional to ensure you're taking advantage of all available deductions and strategies.

## PASSIVE LOSS EXCEPTION

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- If you **don't** qualify as a real estate professional, you may still deduct rental losses under certain conditions
- Must be actively involved in managing the property
- Income limits apply—the deduction phases out as income increases
- This exception is often overlooked but can provide meaningful tax savings for qualifying taxpayers

## COST SEGREGATION STUDIES

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- A cost segregation study breaks out property components to **accelerate depreciation** deductions
- Most beneficial for higher-value properties—the cost of the study needs to be justified by tax savings
- Commonly used with 1031 exchanges and by real estate professionals
- **Important:** This speeds up depreciation but also reduces your tax basis—understand the long-term implications

## QUALIFIED BUSINESS INCOME (QBI) DEDUCTION

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- Rental real estate may qualify for the **QBI deduction**—a deduction on qualifying pass-through income
- **Safe harbor:** Requires maintaining separate books and records, plus meeting an annual hours threshold working on the property
- Income limits apply, but even higher earners may qualify through the **basis test** based on property value
- One of the most commonly missed deductions on tax returns—worth reviewing with your tax professional

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