

## Understanding Capital Gains in Real Estate

When you sell a stock, you owe taxes on your gain — the difference between what you paid for the stock and what you sold it for. The same holds true when selling a home (or a second home), but there are some special considerations.

### How to Calculate Gain

In real estate, capital gains are based not on what you paid for the home, but on its adjusted cost basis. To calculate, follow these steps:

**1. Purchase price:** \_\_\_\_\_

The purchase price of the home is the sale price, not the amount of money you actually contributed at closing.

**2. Total adjustments:** \_\_\_\_\_

To calculate this, add the following:

- Cost of the purchase — including transfer fees, attorney fees, and inspections, but not points you paid on your mortgage.
- Cost of sale — including inspections, attorney fees, real estate commission, and money you spent to fix up your home just prior to sale.
- Cost of improvements — including room additions, deck, etc. Note here that improvements do not include repairing or replacing something already there, such as putting on a new roof or buying a new furnace.

**3. Your home's adjusted cost basis:** \_\_\_\_\_

The total of your purchase price and adjustments is the adjusted cost basis of your home.

**4. Your capital gain:** \_\_\_\_\_

Subtract the adjusted cost basis from the amount your home sells for to get your capital gain.

### A Special Real Estate Exemption for Capital Gains

Since 1997, up to \$250,000 in capital gains (\$500,000 for a married couple) on the sale of a home is exempt from taxation if you meet the following criteria:

- You have lived in the home as your principal residence for two out of the last five years.
- You have not sold or exchanged another home during the two years preceding the sale.
- You meet what the IRS calls “unforeseen circumstances,” such as job loss, divorce, or family medical emergency.