TY 2026

PART 1 OF 2 · THE $500,000 SHIELD

HOME SALE EXCLUSION

The biggest tax-free payday in the code

Up to **$500,000** of profit from selling your main home can be 100% federal-tax-free. It's IRC §121 — and it's not automatic.

HOW MUCH IT SHIELDS

Gain you can wipe off your return when you sell your main home:

SINGLE FILER	MARRIED FILING JOINTLY
$250,000	**$500,000**
of gain — $0 federal tax	of gain — $0 federal tax

It shields **GAIN** — not the sale price. Frozen at these levels since **1997** (never indexed).

PASS THREE TESTS ON SALE DAY

Miss any one and the shield doesn't apply (rare exceptions — see part 2):

OWN it — the ownership test — **2 of 5**
You owned the home for at least 2 years, counted back from closing.

LIVE in it — the use test — **2 of 5**
Your main home for 24 months — not necessarily consecutive months.

WAIT — one shield per 2 years — **2 yrs**
No §121 exclusion claimed on another home sale in the prior 2 years.

ADD IT UP — A MARRIED COUPLE SELLS

$750,000 sale price after costs − **$350,000** purchase + upgrades = **$400,000** the gain → **$0** federal tax owed

Bought $300,000 · added $50,000 of improvements · sold $780,000 minus $30,000 selling costs.
The $400,000 gain sits fully under their **$500,000** shield.

Today's prices blow past a cap frozen in 1997. →
Next: raise your basis, handle a gain over the cap — and dodge the traps.

EGH TAX

TAX PREPARATION & PLANNING

Source: IRS Pub 523 · Topic 701 · IRC §121 · educational content, not individualized tax advice

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PART 2 OF 2 · PLAN THE SALE

HOME SALE EXCLUSION

A cap frozen in 1997 — at 2026 prices

The caps never moved while home values kept climbing — big gains now spill over the line. **Three planner moves protect you.**

1 Raise your basis — receipts are money

Gain = sale price − selling costs − what you put in. Every documented improvement shrinks the gain **before** the shield is even needed.

✓ COUNTS — ADDS TO BASIS	✗ DOESN'T COUNT
· Addition, deck, finished basement	· Fixing leaks & repainting
· New roof, windows, HVAC, water heater	· Routine maintenance & upkeep
· Kitchen or bath remodel	· Anything repaired, not improved
· Landscaping, driveway, fence	· The value of your own labor

Selling costs — agent commission, legal fees — also shrink the taxable gain.

2 Over the cap? Only the spill is taxed

The excluded slice never touches your return — the rest is long-term gain.

Example: married couple, $600,000 gain

$500,000 excluded — tax: $0	$100,000

The $100,000 spill is long-term gain — **15%** for most couples = **$15,000**.

Effective rate on the whole $600,000: 2.5%. Add 3.8% NIIT only above $250k MAGI.

3 Sold "too early" or widowed? Escape hatches

Two cases still get shelter when the standard tests fail:

Job move, health, or the unforeseen

A prorated cap: 12 of 24 months still shelters $125k single / $250k married.

Surviving spouse — a 2-year window

Sell within 2 years of your spouse's death and keep the full $500,000.

MIND THE TRAPS

- Rental or home-office depreciation is never shielded — taxed separately, up to 25%.
- Rented it out **before** moving in? Post-2008 rental years shrink the shield pro-rata.
- Got a 1099-S at closing? You **must report** the sale (Form 8949) — even at $0 tax.

THE BOTTOM LINE

The shield is **use-it-right, not automatic.** Keep every improvement receipt, watch the 2-of-5 clock — and price the sale with your cap in mind.

Source: IRS Pub 523 · Rev. Proc. 2025-32 · Treas. Reg. 1.121-3 · state tax may differ · educational content, not individualized tax advice