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CAN YOU DEDUCT LOSSES FROM RENTING YOUR OLD HOME?

By Victor Sy, CPA

If you have to **move but can't sell your home** in this slow real estate market, what are your options? Well, **renting** comes to mind. Paying for another mortgage on your new home would be a financial challenge. But if you do rent (or try to rent out), can you deduct rental losses on your old home?

Tax laws state that if you move out from your home and rent it out, try to rent it, or list it with a realtor for rent, your property is converted to income-producing property. Therefore, *yes you can*. **Expenses related to the property are deductible, even if the property is *not* actually rented for several years or is *never* actually rented.**

This could be **tax shelter** for you: if your home is rented, your gross rental income is offset by mortgage, property tax, insurance, utilities and maintenance. It could be a wash. But then comes depreciation that typically produces a net loss. You have converted your home into a rental property and, therefore, can deduct the rental loss (there are, of course, passive losses that you have to deal with, but that's another issue).

In a recent Tax Court case, a taxpayer named Bonds relocated from Kansas City to Minneapolis. She **rented** her Kansas City house to various tenants through 2004 or 2005. She was **not** able to rent it out after that but she **continued to deduct her rental losses**. Bonds attributed her failure to rent the property to a number of factors, including the economy and the property's location.

Bonds claimed rental losses from advertising, auto, travel, cleaning, maintenance, insurance, mortgage interest and taxes, and depreciation. IRS **disallowed** the rental losses, taking the position that the Kansas City house was not held for the production of income but was rather a **second home**. Taxpayer went to Tax Court to challenge that disallowance.

Bonds won. The Tax Court held that she **converted** her old Kansas City house from personal use to property held for production of income when she relocated to Minnesota. She rented the property to various tenants between 2004 and 2005. While Bonds did not derive any subsequent rental income, she kept the property hoping to sell at a gain when the market recovers. The Tax Court said that the **home was also held for income** during 2006 and 2007 even when it was **not** actually rented. It also held that because Bonds participated in a significant and bona fide sense in making management decisions, she satisfied active participation standards in 2006 and 2007 and was therefore **entitled to rental losses**. Note however that the Tax Court **disallowed many expenses because she failed to keep adequate records of certain expenses**.

In summary:

- Yes, you **can deduct losses from renting your old home**.
- Yes, you **can deduct expenses that you can support** - mortgage, property tax, insurance.
- No, you cannot deduct expenses that you cannot support, including repairs with no receipt.