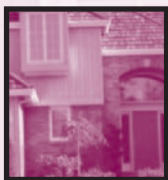


RENTAL PROPERTY



**Understanding the tax benefits
of rental property ownership**

Rental Property

Owning and renting property is common for many individuals. While the rental income and/or capital gains from owned property can be a financially rewarding endeavor, the IRS rules and regulations can be very complex.

This Rental Income brochure summarizes the most common forms of rental income, allowable expenses and their tax treatment.

The worksheet on the reverse side should help you document your rental income and identify deductible expenses from rental activities.

Rental Property Tax Law

Special tax laws have been created within the Tax Code to address rental income and losses. Generally, rental income is deemed “Passive” income within the IRS. This is done to distinguish rental income from “Earned” or “Ordinary” income like your salary or wages. This “passive” activity requires separate tax forms be filed and it limits your ability to net losses on rental activity against other types of income like your wages. On the other hand, “Passive” income is not subject to employment taxes (Social Security and Medicare). However, not all rental activity must by its nature be passive. Exceptions are renting vacation property and rental activity in which you are actively involved. The rules are complex, so it is always a good idea to discuss your situation.

Rental Income

What is Rental Income?

Rental income is any amount of money you receive or accrue as payment for the use of property. You must include:

- rent payments
- payments made to you by your lessee (renter) for any of your expenses
- any payment to you by a lessee as consideration for abandoning the lease agreement
- property taxes paid by your tenant on behalf of the landlord
- deposits from your renters

- improvements made to the property by a lessee in lieu of rent payments — These are included as gross income at the fair market value of the improvements at time of improvement

What isn't Rental Income?

There are some forms of income from rental property that may be excluded such as:

- Rental income if a property is rented less than 14 days per year (e.g. Vacation Home Rental)
- Improvements made by your Lessee while renting from you that will belong to your property when the lease expires or if the lease is terminated prior to expiration

Rental Expenses

Rental expenses directly related to the property that produces rent income are deductible from gross rental income to derive your adjusted gross rental income. Use the worksheet on the reverse side to assist you in identifying, tracking and documenting your gross rental income, deductions and adjusted gross income.

Other Rental Income

Vacation Home Rental

Owning a vacation home can bring tax advantages for you, but the rules can be a little complex depending on the amount of personal and rental use of your home. It is best to review your vacation home plans on a regular basis to help maximize your tax advantages. Briefly, the rules are:

- If you don't rent out your vacation home, you can deduct mortgage interest and real estate taxes.
- If you rent out your vacation home for 14 days or less, you can deduct the mortgage interest and the real estate taxes and the rental income is tax-free. You may not deduct any expenses associated with renting out the home, however.
- If you rent out the home 100% of the time and there is no personal use, the vacation home is considered a rental property. In this case you may deduct interest, taxes, operating expenses, depreciation and possibly rental losses up to \$25,000.

- If you rent out your vacation home for more than 14 days, and also use the home personally the rules regarding personal use and what you can deduct are very complex and should be discussed to determine your best tax opportunities.

Rental of Personal Property

If you rent personal (non-real estate) property through a trade or business:

- This rental income is treated as self-employment income and is subject to self-employment taxes of 15.3%
- You must record and file this income on a Self-employed Income Schedule, and not as Rental Income

If you rent personal property with the rental of real estate the personal property rent is not subject to the self-employment tax. Other rent income excluded from the self-employment tax are:

- Rental income from a mobile home park
- Rental income from self-storage units
- When rental activity is not conducted as a trade or business on a regular and consistent basis

In these cases rent income is reported as Other Income.

Selling Your Rental Property

Any time you sell property you are required to calculate the gain or loss on the sale for tax purposes. When you sell property that you have rented, even if only part of the property was rented, the calculation of gain or loss becomes more complicated. Any depreciation taken on the property must be accounted for when determining the actual gain or loss. For instance, assume you sell a condo for \$200,000 that you bought for \$100,000; also assume you have rented the condo and depreciated \$10,000 of the cost on your rental tax filings. Your taxable gain on the sale would be \$110,000 (\$200,000 minus \$100,000 cost plus the \$10,000 depreciation). Fortunately, long term capital gain tax rates are lower than in the past, but this depreciation recapture can be quite a tax surprise.

Rental Property Tracking Worksheet

(Use the worksheet below to record and track your rental property income and expenses. Allowable expenses may be deducted from your gross rental income to derive your adjusted gross rental income. Tracking your rental income and expenses quarterly will assist in deriving your estimated quarterly taxes owed. Use a separate worksheet for each rental property)

Property Name/Address: _____

	1 st Qtr.	2 nd Qtr.	3 rd Qtr.	4 th Qtr.	Total Year
INCOME					
Rents Received					
Deposits Received					
Other:					
Total Income					
EXPENSES					
- Advertising					
- Auto Travel Mileage					
- Cleaning/Maintenance					
- Electricity					
- Fuel					
- Homeowners Assoc. Dues					
- Insurance					
- Legal & Professional					
- Management Fees (Commissions)					
- Mortgage Interest					
- Other Interest					
- Real Estate Taxes					
- Refunds					
- Repairs					
- Painting					
- Plumbing					
- Electrical					
- Appliances					
- Other Repairs					
- Rubbish Hauling/Trash					
- Supplies					
- Telephone					
- Travel Expense (Detail)					
- Wages/Labor					
- Water/Sewer					
- Yard/Snow Removal					
- Other:					
- Other:					
- Other:					
Total Expenses					
Net Income (Income- Expenses)					

This publication provides only summary information regarding the subject matter. Please call with any questions on how this information may impact your situation.