

Internal Revenue Service

Department of the Treasury
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Person To Contact:
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Telephone Number:

In Re:

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March 19, 2008

LEGEND

Taxpayer A:
Taxpayer B:
Residence X:
Residence Y:
Residence Z:
Date 1:
Date 2:
Date 3:
Date 4:
Date 5:
Date 6:

Dear _____ :

This responds to your letter dated October 5, 2007, requesting a ruling on whether you are eligible to exclude gain from the sale of a residence under § 121(c) of the Internal Revenue Code.

FACTS

We rely on the facts set forth in Taxpayers' submissions dated October 5, 2007, November 27, 2007, January 31, 2008, February 19, 2008, and March 11, 2008.

Taxpayer A purchased Residence X as her and her two daughters' principal residence and moved in on Date 1. Taxpayer A then purchased Residence Y as her and her two daughters' principal residence and moved in on Date 2. As of Date 2, Taxpayer A and Taxpayer B were neither married nor considering marriage. Taxpayer A sold Residence X on Date 3. As of Date 3, Taxpayer A owned and used Residence X as her principal residence for more than two years during the five-year period preceding the sale.

Taxpayer A excluded gain realized on the sale of Residence X from her federal income tax return.

Taxpayer A and Taxpayer B were engaged on Date 4, and married on Date 5. On Date 5, Taxpayer A and her two daughters moved into Residence Z, which was Taxpayer B and his son's principal residence, and began to use Residence Z as her principal residence. Taxpayer A sold Residence Y on Date 6. As of Date 6, Taxpayer A owned and used Residence Y as her principal residence for more than two years during the five-year period preceding the sale. The sales of Residence X and Residence Y occurred within two years.

Taxpayers represent that Residence Y is not suitable for their blended family. Taxpayer A has two pre-adolescent daughters, and Taxpayer B has one adolescent son from their previous respective marriages. If the blended family moved into Residence Y, the son and the daughters would not have adequate privacy due to the layout of Residence Y. In addition, by moving into Residence Z, all the children were eligible to stay in the schools they attended prior to the marriage. If the blended family moved into Residence Y, Taxpayer B's son would have to move to a new school because of enrollment policies.

Taxpayers request that Taxpayer A be entitled to exclude gain from the sale of Residence Y under the reduced maximum exclusion provisions of § 121(c).

LAW AND ANALYSIS

Section 121(a) provides that gain from the sale of property is not included in gross income if, during the five-year period ending on the date of the sale, the taxpayer has owned and used the property as the taxpayer's principal residence for periods aggregating two years or more.

Section 121(b)(1) provides that the maximum exclusion amount is \$250,000. In the case of a husband and wife, the maximum exclusion amount is \$500,000 only if (1) a husband and wife file a joint return for the year of the sale, (2) each spouse meets the two-year use test, (3) at least one of the spouses meets the two-year ownership test, and (4) neither spouse used the § 121 exclusion during the last two years. See § 1.121-2(c) of the Income Tax Regulations.

Section 121(b)(3) provides that subsection (a) shall not apply to any sale if, during the two-year period ending on the date of the sale, there was any other sale or exchange by the taxpayer to which subsection (a) applied.

Section 121(c) provides for a reduced maximum exclusion when a taxpayer fails to satisfy the ownership and use requirements of subsection (a), and/or the application limitation of subsection (b)(3), if the primary reason for the sale is the occurrence of employment, health, or unforeseen circumstances.

The reduced maximum exclusion is computed by multiplying the applicable maximum exclusion by a fraction. The numerator of the fraction is the shortest of the following periods: (1) the period of time that the taxpayer owned the property during the five-year period ending on the date of the sale; (2) the period of time that the taxpayer used the property as the taxpayer's principal residence during the five-year period ending on the date of the sale; or (3) the period of time between the date of a prior sale or exchange of property for which the taxpayer excluded gain under § 121 and the date of the current sale. The numerator of the fraction may be expressed in days or months. The denominator of the fraction is 730 days or 24 months (depending on the measure of time used in the numerator). See § 1.121-3(g).

Section 1.121-3(b) provides that all the facts and circumstances of a sale will determine whether the primary reason for the sale is the occurrence of unforeseen circumstances. Factors that may be relevant in determining the primary reason for a sale include the following: (1) the sale and the circumstances giving rise to the sale are proximate in time; (2) the suitability of the property as the taxpayer's principal residence materially changes; (3) the taxpayer's financial ability to maintain the property is materially impaired; (4) the taxpayer uses the property as the taxpayer's residence during the period of the taxpayer's ownership of the property; (5) the circumstances giving rise to the sale are not reasonably foreseeable when the taxpayer begins using the property as the taxpayer's principal residence; and (6) the circumstances giving rise to the sale occur during the period of the taxpayer's ownership and use of the property as the taxpayer's principal residence.

Section 1.121-3(e)(1) provides that a sale is by reason of unforeseen circumstances if the primary reason for the sale is the occurrence of an event that the taxpayer could not reasonably have anticipated before purchasing and occupying the residence. Section 1.121-3(e)(3) states that the Commissioner may issue rulings addressed to specific taxpayers identifying events or situations as unforeseen circumstances with regard to those taxpayers.

Based on the facts, representations, and the relevant law, we conclude that Taxpayer A's primary reason for the sale of Residence Y was the occurrence of unforeseen circumstances. Consequently, even though Taxpayer A sold Residence Y within the two-year period from the sale of Residence X, to which § 121 applied, Taxpayer A is

granted permission to exclude gain from Residence Y up to the reduced maximum exclusion amount under § 121(c).

Caveats

Except as expressly provided, we express no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter ruling must be attached to any income tax return to which it is relevant. Alternatively, if Taxpayers file a return electronically, Taxpayers may attach a statement to the return that provides the date and control number of the letter ruling.

The ruling contained in this letter is based upon information and representations submitted by Taxpayers and accompanied by a penalty of perjury statement executed by Taxpayers. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,

George F. Wright
Senior Technician Reviewer, Branch 5
Office of Associate Chief Counsel
(Income Tax & Accounting)