



CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

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Attention:

Dear Representative Fletcher:

I'm responding to your November 8, 2024, inquiry regarding the rules for excluding from income up to \$500,000 of gain on the sale of a house. The inquiry asked whether there is an exclusion for a taxpayer who cannot use the property as their principal residence because of a natural disaster.

Under Section 121(a) of the Internal Revenue Code (Code), a taxpayer may exclude up to \$250,000 (\$500,000 for certain joint returns) of gain on the sale or exchange of property. This is only if the taxpayer owned and used it as their principal residence for at least 2 years during the 5-year period ending on the date of the sale or exchange. Section 121(b)(3) provides that the full exclusion is available only once every two years.

Under Section 121(c) of the Code and Section 1.121-3 of the Income Tax Regulations (Regulations), a taxpayer who does not satisfy the ownership and use requirements of Section 121(a) or the 2-year limitation of Section 121(b)(3) may be able to claim a reduced exclusion if their home is sold or exchanged due to a change in place of employment, health, or unforeseen circumstances.

A sale or exchange is considered to be of unforeseen circumstances if a natural disaster resulting in a casualty occurs during the period the taxpayer owned and used the property as their principal residence according to Section 1.121-3(e)(2)(ii) of the Regulations.

The reduced maximum exclusion is computed by multiplying the maximum dollar limitation of \$250,000 (\$500,000 for certain joint filers) by a fraction.

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If a taxpayer did not use the property as their principal residence at any time during the 5-year period ending on their date of sale, they would not qualify for the full exclusion under Section 121(a) or the reduced exclusion under Section 121(c) and Section 1.121-3, regardless of whether a natural disaster prevented the use of the property as a residence.

More information on the Section 121 exclusion may be found in Publication 523, which may be accessed at <https://irs.gov/pub523> on our website at www.irs.gov.

I hope this information is helpful. If you have any questions, please call me or
, at .

Sincerely,

Shareen S. Pflanz
Chief, Branch 8
Office of Associate Chief Counsel
(Income Tax & Accounting)