REAL ESTATE TAX REFERENCE GUIDE

REPS Status, Passive Loss Limitations, and Short-Term Rental Rules (IRC § 469)

1. STATUTORY RULES FOR REAL ESTATE PROFESSIONAL STATUS (REPS)

The 750-Hour Rule:
You must perform more than **750 hours** of personal services during the tax year in real property trades or businesses in which you materially participate.
**Note: Spouses cannot combine hours to meet the 750 threshold on a joint return; one individual spouse must qualify independently.*

The More-Than-50% Rule:
Your personal services in real property trades or businesses must account for **more than 50%** of your total working hours across **all** employments, trades, or businesses for the entire tax year (including non-real estate W-2 jobs).

2. MATERIAL PARTICIPATION SAFE HARBORS (IRC § 469)

Even if you pass the 750-hour and 50% rules, you must still prove you **materially participate** in your specific rental properties to unlock ordinary loss deductions. You must satisfy at least one of these three primary safe harbors every single tax year:

- **The 500-Hour Test:** You participate in the activity for more than 500 hours during the year.
- **The 100-Hour / Most Test:** You participate for more than 100 hours, and your participation is not less than any other individual.
- **The Sole Participant Test:** Your participation constitutes substantially all of the participation in the activity by any individual.

3. REAL ESTATE DEDUCTION & STR STRATEGY MATRIX

Taxpayer Strategy / Status	MAGI Income Phase-Out Limits	Max Annual Loss Offset Allowed	7-Day or Less Rule Applicability
Passive Investor (LTR) *Standard Long-Term Rentals*	**Full allowance:** ≤$100,000 MAGI. Phases out dynamically between **$100,000 – $150,000**.	**$25,000 Maximum Cap** per year (requires active participation). Drops to **$0** if MAGI is over $150,000.	**Does not apply.** Stays strictly governed by baseline passive activity loss restrictions.
Real Estate Professional (REPS) *IRC § 469(c)(7)*	**No Income Limit.** The $100k–$150k passive activity phase-out is completely bypassed.	**Unlimited Ordinary Losses.** Allows 100% of rental losses to offset W-2, business, and ordinary income.	**Does not apply.** Governed instead by the 750-hour and >50% aggregate working hour tests.
Short-Term Rental Loophole *Treas. Reg. § 1.469-1T(e)(3)*	**No Income Limit.** The $100k–$150k passive activity phase-out is completely bypassed.	**Unlimited Ordinary Losses.** Can offset active W-2 and business income without needing REPS designation.	**Mandatory Element.** Average customer stay must be **7 days or less** to escape the 'rental activity' definition.

4. CRITICAL IRS AUDIT TRAPS & DISALLOWANCE TRIGGER POINTS

- **The Full-Time W-2 Job Conflict:** Working a 40-hour/week non-real estate job requires working 2,001+ hours in real estate to pass the 50% rule. The IRS heavily scrutinizes and routinely disallows this setup.
- **Omission of the § 1.469-9(g) Grouping Election:** The IRS evaluates hours *per individual property* by default. Without a formal, filed election to group all rental entities as a single activity, the REPS claim will be systematically rejected.
- **Excluded 'Investor' and Secondary Hours:** Travel time, educational seminars, analyzing prospective deals, organizing financial statements, and being 'on-call' are completely excluded from the 750-hour count.
- **The STR Material Participation Illusion:** Under the 7-day STR loophole, if a property manager or cleaning crew logs more individual hours than the owner, the IRS will disallow ordinary losses unless the owner clears the 100-hour threshold *and* out-works everyone else.
- **The 5% Real Estate Employee Threshold:** Hours worked as an employee in a real estate trade (e.g., brokerage, property management, construction) do not count toward REPS unless you own at least **5%** of the business entity.
- **Reconstructed Ballpark Guesstimates:** Post-facto log sheets created months after the tax year are consistently thrown out by the US Tax Court. Logs must be contemporaneous, detailing dates, precise descriptions, and supporting trail records.

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