

Selling Your Home as an Installment Sale

What Is An Installment Sale?

According to the Internal Revenue Service (IRS), an Installment Sale is the sale of an asset where the seller receives at least one payment after the tax year of the sale. Rather than receiving the total contract price for the asset at one time, the seller spreads the payment of the property over time using a specific Installment Sale documentation such as a deed of trust or mortgage (depending on the state) and note that specifies the terms of the repayment. These types of transactions have been done for many years. In fact, the IRS has a detailed publication that explains all of the tax benefits. Go to <https://www.irs.gov/pub/irs-pdf/p537.pdf> to be directed to the IRS website to view IRS Publication 537. Many people refer to Installment Sales as selling on terms, seller financing or owner financing.

How An Installment Sale Works

With an Installment Sale, the buyer makes payments to the seller over time, rather than handing over a lump sum at closing. The buyer's obligation to make future payments to the seller will be spelled out in a deed of trust or mortgage and note according to the sales contract between the buyer and seller, as any other bank or mortgage company would require. This way the buyer's promise to pay the seller is secured by the property. In other words, if the buyer does not pay, the seller can foreclose and get the property back and sell it again.

Benefits Of An Installment Sale

- An Installment Sale is best used when selling a property with no mortgage. In this case, the seller would like to sell their property fast, at a higher sales price, as opposed to discounting the sale price for an all cash offer.
- The Installment Sale can create a steady stream of income over a number of years for the seller and allow the taxable gain on the sale to be spread out over those same years instead of immediately upon the sale.
- It is also very popular with landlords that want to keep the cash flow but eliminate the problems of being a landlord such as, dealing with tenants, vacancies, making repairs or capital improvements, etc.
- It is a great alternative to a cash sale because the seller can get more money for their property and earn interest on the money as well. The interest is taxed separately at ordinary tax rates. This is ideal for a seller that doesn't have a

purpose for the money if they were to sell the property for cash.

- Many aging sellers have also seen the advantages if Installment Sale for their heirs. Their heirs would much rather inherit a monthly cash flow without having to deal with real property and tenants.

- An Installment Sale also provides an easy transition for any heirs upon the death of the seller, as many sellers do not want their heirs to have to deal with managing a property and dealing with tenants upon their death.

- Some sellers have even said that they do not want their heirs to inherit a lump sum but prefer they receive monthly payments so the money will last longer.

Tax Benefits of Installment Sale

Installment Sales are a popular tax planning technique for real estate owners. Although you'll still owe tax under the Installment Sale method, you're in line for three key tax breaks.

An Installment Sale method allows for the deferral of capital gains in future tax years. Installment Sales require the buyer to make regular payments. Typically, most Installment Sales call for monthly payments, but can be structured as quarterly or annual payments as well.

An Installment Sale can help sellers keep their income within a desired tax bracket by spreading out their income. Installment Sales can keep capital gains in a lower tax bracket. They can also help individuals either lower or avoid higher Medicare Part B premiums, net investment income taxes, or alternative minimum taxes. These types of sales can also help prevent Social Security benefits from being taxed by keeping income lower. The benefits of not recognizing the entire sale can help ensure an individual can still take the full amount of student loan interest deduction, itemize deductions, or take other deductions that are limited by income. Installment Sale can be a huge benefit for landlords. If a landlord has owned a property for many years, they have probably depreciated it to the extent that they have zero basis in it and any money they receive in a cash sale would be taxable and could put them into a higher tax bracket. This is what makes the Installment Sale so attractive for landlords that like cash flow but are at a stage in their life that they do not want to deal with tenants or leave rental property to their heirs to have to deal with.

Closing Process With Installment Sale

When closing a transaction using the Installment Sale, the closing process is basically handled the same way as any other real estate transaction. An attorney or title company will handle the closing to protect the buyer and seller. A title report will be issued to insure the property is clear of any liens or judgements and/or back taxes. The attorney or title company will also insure that the seller owns the property and can convey the property. They will also require the buyer to sign the loan documentation for the Installment Sale (which may include a note, deed of trust or mortgage) which obligates the buyer.