

REAL ESTATE PROFESSIONAL

TAX PAYER ACTIVITY RESOURCE



- IRS Accepted RE Pro Activities •

Part 1
The IRS Material Participation

Part 2
RE Pro Qualifiers

Part 1

This is a discussion of seven areas the IRS uses to address Material Participation

Development or Redevelopment:

The acts associated with building a property on a bit of land...the acts associated with repurposing or converting something or a property to rental. This requires a lot of due diligence, speaking with contractors and such.

Taking a long-term rental and converting it into short term rental use, the supervision of construction of a new build property with the intent of placing it into rental service, the acts associated with the acquisition of a residential property with the intent to convert it to a rental Any act that assists converting from long term to short term rental

Constructs or Reconstruct it:

This is the actual act of building or remodeling or rehabbing a property. This would be dealing with the contractors this would be dealing with the various people actually touching the properties and or actually working on property yourself.

Obtaining permits, dealing with architects, doing design work, doing interior design work, doing anything to improve the rentability of the property or being actively involved in that.

The IRS would prefer material participation to be actual physical contact with the property, however many of the cases I've read they will except phone calls and video and zooms and all the rest of it as material participation.

Acquires it:

This one's kind of obvious. Anything that you do in the performing of due diligence research before you purchase a property (whether you actually purchase it or not) goes into this category. This would include dealing with real estate agents, wholesalers management companies, appraisers, home inspection people, city inspection, and things of that nature.

Converts it:

This is converting a room in your home to a rental real estate property. This would be the conversion of a storage facility into a residence. This would be acquiring a single-family home and putting it into service, converting it, and anything done to make the property more of a rental.

Rents or leases it:

This part gets kind of tricky if you have managers on the ground. They are doing a lot of the work for you however if you retain refusal rights and if they have to get your permission, you're participating in the renting and/or leasing of your properties.

This also has to do with conversations with your management company about what to rent the property for, how to lease the property and how to market the property.

Operates or manages it:

This would be specifically dealing with the tenants leasing documents etc. This is the ongoing managing of the property, dealing with complaints, dealing with ongoing repairs etc. as you would likely have a property manager involved.

It's important for you to document that you are materially participating by providing specific input permissions as to what exactly is being done with your property. This also would include collecting rents directly and include anything where you are tenant facing in your participation.

Brokers it:

Essentially the act of selling or the act of acting as a broker in the real estate world. If you do hard money loans this is very likely to qualify in this area. (Check with your tax or legal team).

Part 2

Taxpayers often ask "what must I do to qualify as a real estate professional and make my real estate activities a business?" Or "how do I make my real estate activities active?"

To qualify, there are a few things you **must** do.

1. You must participate in real estate **51%** of your time. If you work full-time, this is extremely difficult to prove.
2. You must have **at least 750 hours** of material participation. Most tax advisors would prefer to see more than that because the IRS loves to get picky and disqualify certain activities.
3. You must have a **log**. This log will provide details proving or stating the property address, what the participation or activity was, and how many hours you spent on it. The IRS does not require any particular format. Most people prepare a spreadsheet.
4. In addition, you must include a form that **aggregates** all of your activities and properties.

There are specific IRS instructions regarding material participation. The following pages specifically address these instructions.

Disclaimer

We are not Certified Public Accountants or Tax attorneys. The information shared in this document is publicly available information. Before applying or using any of the information provided, you should consult with your tax and legal professional.