

Short Term Rental Tax Strategy: New IRS Compliance Rules and What Investors Need Before Year End

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Short term rental tax strategies have become extremely popular among real estate investors, especially those seeking to reduce high taxable income through bonus depreciation and accelerated write offs. However, the IRS is intensifying its examination of short term rentals, and many investors are discovering that they do not meet the material participation or rental activity requirements they thought they qualified for.

Understanding the Short Term Rental Definition

To qualify for non passive treatment, your property must meet IRS requirements that include:

- An average stay of seven days or less
- Or, if longer than seven days, you must provide substantial services similar to a hotel
- Or, you must meet one of the seven material participation tests

Taxpayers often fail the average stay calculation because they do not track the average length of each reservation. One longer reservation can shift the property

out of short-term rental status for the entire year.

Material Participation Requirements

To qualify, you must be able to prove you personally spent significant time managing the rental. Records such as calendars, emails, guest messages, repair logs, and cleaning oversight are often requested during audits. If a management company or co-host performs most of the work, the IRS will could classify the activity as passive.

Why the IRS Is Increasing STR Audits

The IRS is targeting STRs because:

- Many taxpayers cannot substantiate material participation
- Bonus depreciation makes STRs highly valuable audit targets
- Third-party management complicates compliance
- Investor interest in STRs has increased dramatically

This heightened scrutiny means taxpayers must build a defensible position now, before year end.

Year End Planning for STR Owners

There is still time to strengthen your STR tax position before December 31. Investors should:

- Review their average stay calculations
- Document participation hours with detailed logs
- Confirm that their STR qualifies under IRS definitions
- Evaluate whether a purchase or renovation can be placed in service before year end
- Ensure short term rental licenses and local requirements are updated

If you want to protect your hard earned dollars and ensure your STR strategy can withstand IRS review, our team at Strategic Tax Planning can conduct a detailed compliance analysis before the year closes.