

REAL ESTATE MATTERS: KNOW THE TAX RULES

Taxes are an important part of the decision to own real estate. Here's a brief overview of tax benefits you can realize while you own real property, as well as when you sell or otherwise dispose of the property.

Current expenses. As a rental property owner, you can deduct current expenses to offset the tax you owe on the rent you receive. For instance, you can write off mortgage interest, property taxes, repairs, and expenses of maintaining your property. The cost of capital improvements is generally added to your basis, providing a benefit when you sell. Be aware that passive activity rules may limit your ability to claim current annual losses.

Depreciation. Depreciation lets you convert the purchase price of your rental property into an expense over the property's expected life. The recovery period for residential buildings is 27½ years, while commercial buildings use a 39-year period. Some qualified improvements may be expensed over a shorter time.

Capital gain. The sale of real estate is generally taxed under capital gain rules. If you sell rental property you've held for longer than one year for more than you paid for it, the gain is taxed at rates up to 15% (20% if you're in the top ordinary income tax bracket). However, you may have to recapture some of the depreciation expense you claimed over the time you owned the property. That can mean part of your gain may be subject to higher tax rates. Losses can offset capital gains from sales of other assets.

Like-kind exchange. Instead of selling your property, you might arrange a like-kind exchange under Section 1031 of the federal income tax code, where you "swap" your property for replacement property. If certain timing and other requirements are met, you can defer tax on part or all of the transaction.

Please contact us to discuss these and other tax-saving opportunities.