

Tax Strategies for Real Estate Investors

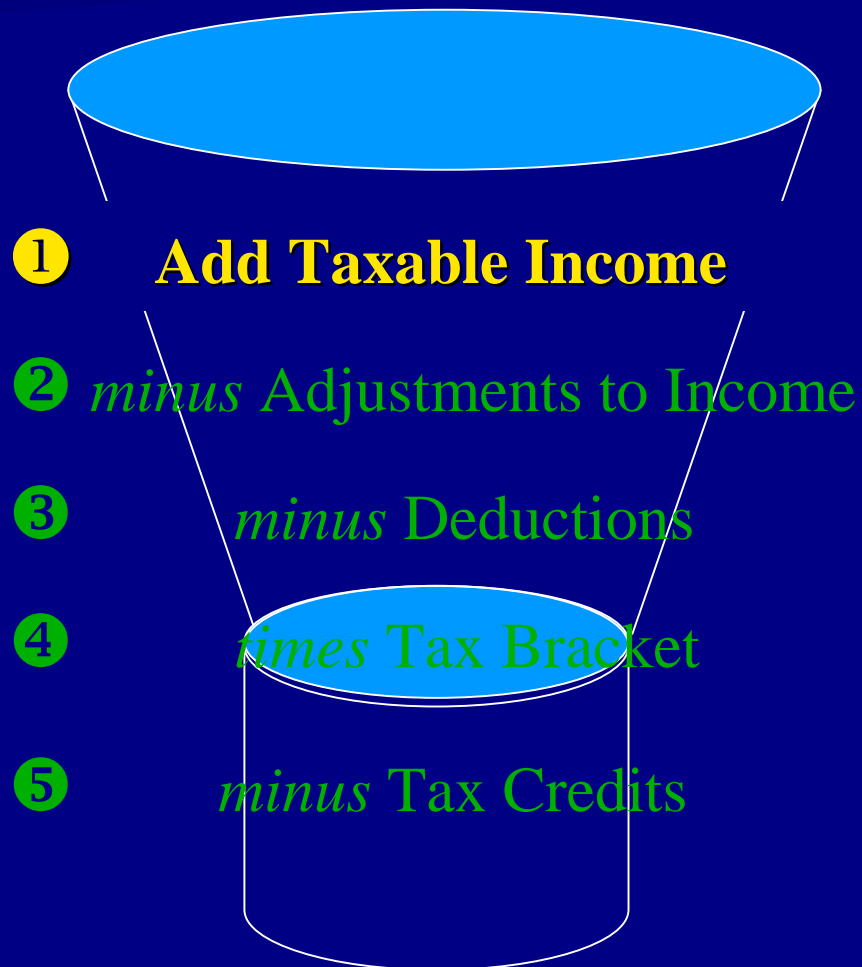
The “Secret” to Beating the IRS

“There is nothing wrong with a strategy to avoid the payment of taxes. The Internal Revenue Code doesn’t prevent that.”

William H. Rehnquist

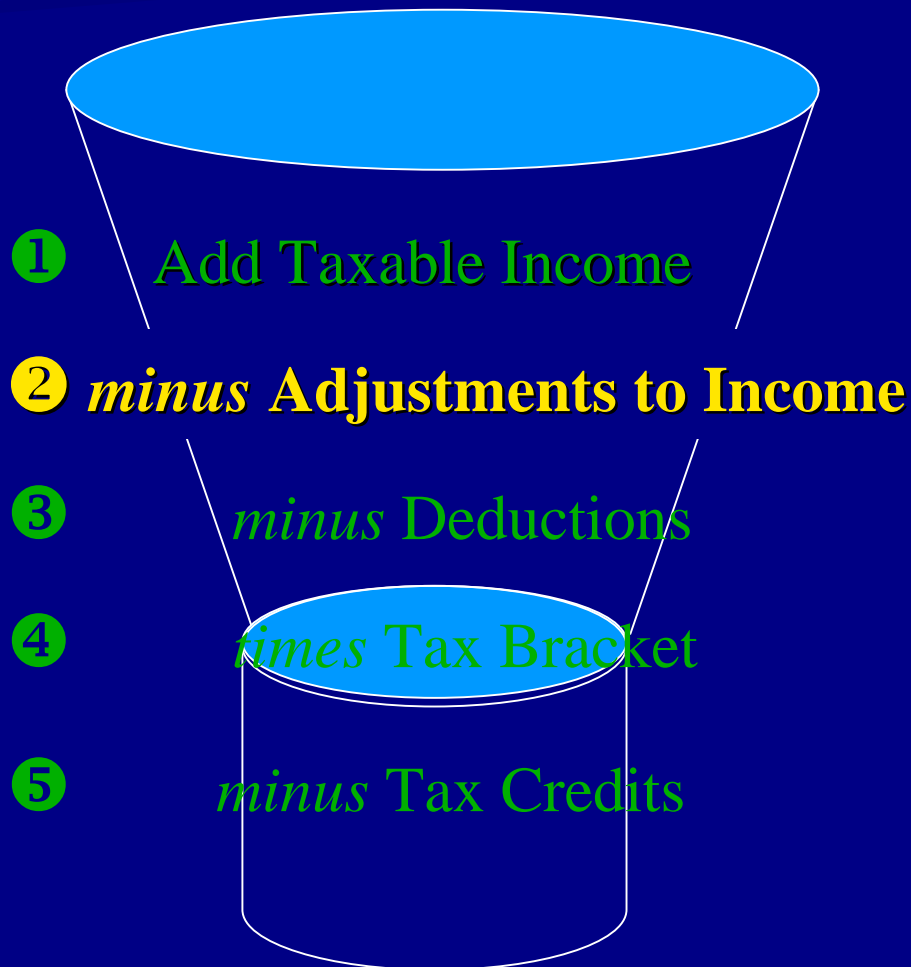
1. Tax planning is financial defense
2. Tax planning guarantees results

Taxable Income



- Earned income
- Interest/dividends
- Capital gains
- Pension/IRA/Annuity
- Rent/royalty
- Alimony
- Gambling winnings
- Illegal income

Adjustments to Income



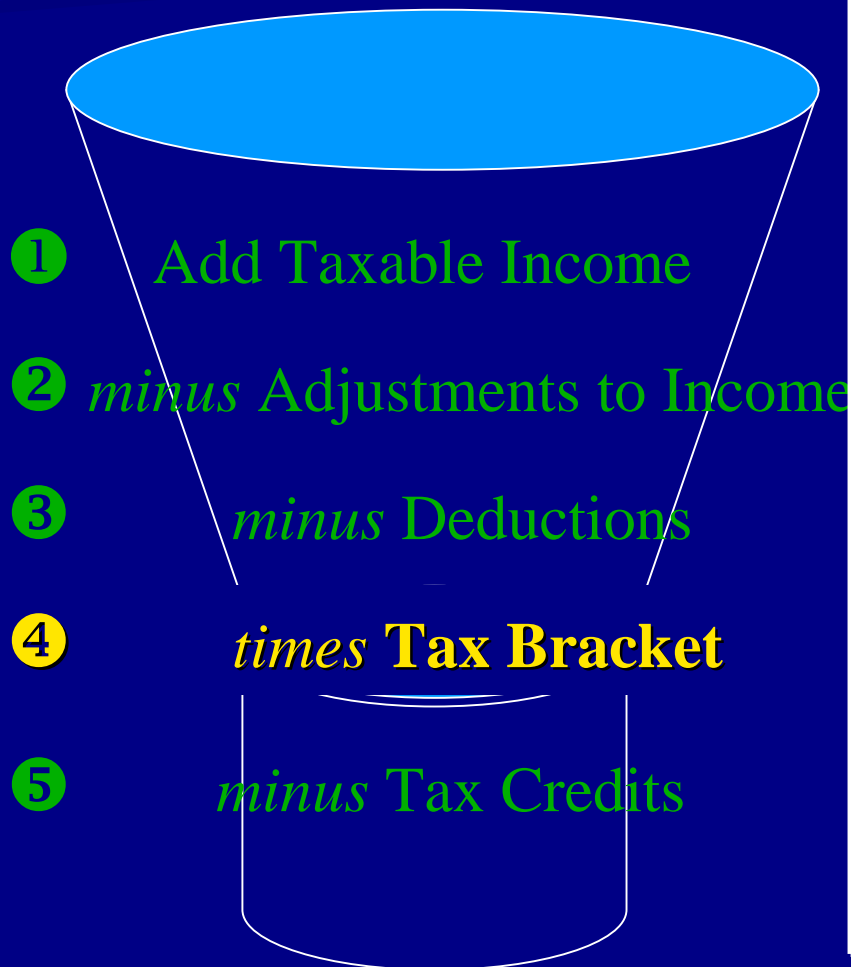
- IRA contributions
- Moving expenses
- ½ SE tax
- SE health insurance
- Keogh/SEP
- Alimony
- Student loan interest

Deductions/Exemptions

-
- ① Add Taxable Income
 - ② *minus* Adjustments to Income
 - ③ *minus* **Deductions/Exemptions**
 - ④ *times* Tax Bracket
 - ⑤ *minus* Tax Credits

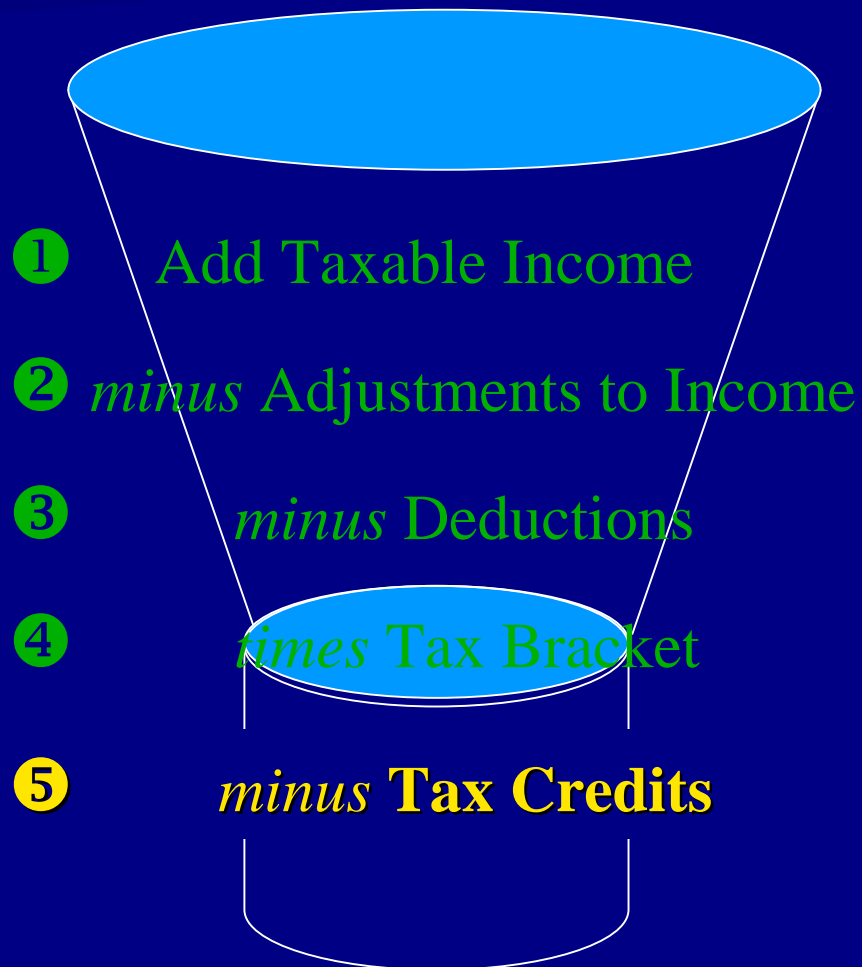
- Medical/dental
- State/local taxes
- Foreign taxes
- Interest
- Casualty/theft losses
- Charitable gifts
- Miscellaneous itemized deductions

Tax Brackets



Rate	Single	HoH	Joint
10%	0	0	0
15%	8,026	16,051	16,051
25%	32,551	43,651	65,101
28%	78,851	112,651	131,451
33%	164,551	182,401	200,301
35%	357,701	357,701	357,701

Tax Credits



- Family credits
- Education credits
- Foreign tax
- General business
- Low-income housing
- Renovation

Two Kinds of Dollars

-
- ① Add Taxable Income
 - ② *minus* Adjustments to Income
 - ③ *minus* Deductions
 - ④ *times* Tax Bracket
 - ⑤ *minus* Tax Credits

Pre-Tax Dollars

After-Tax Dollars

Keys to Cutting Tax

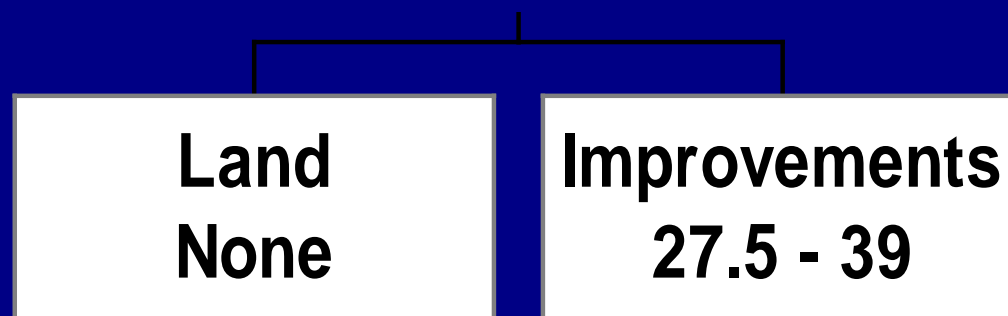
“You lose every time you spend after-tax dollars that could have been pre-tax dollars.”

1. Earn as much nontaxable income as possible
2. Make the most of adjustments/deductions/credits
3. Shift income to later years and lower-brackets

Misunderstanding Audit Odds

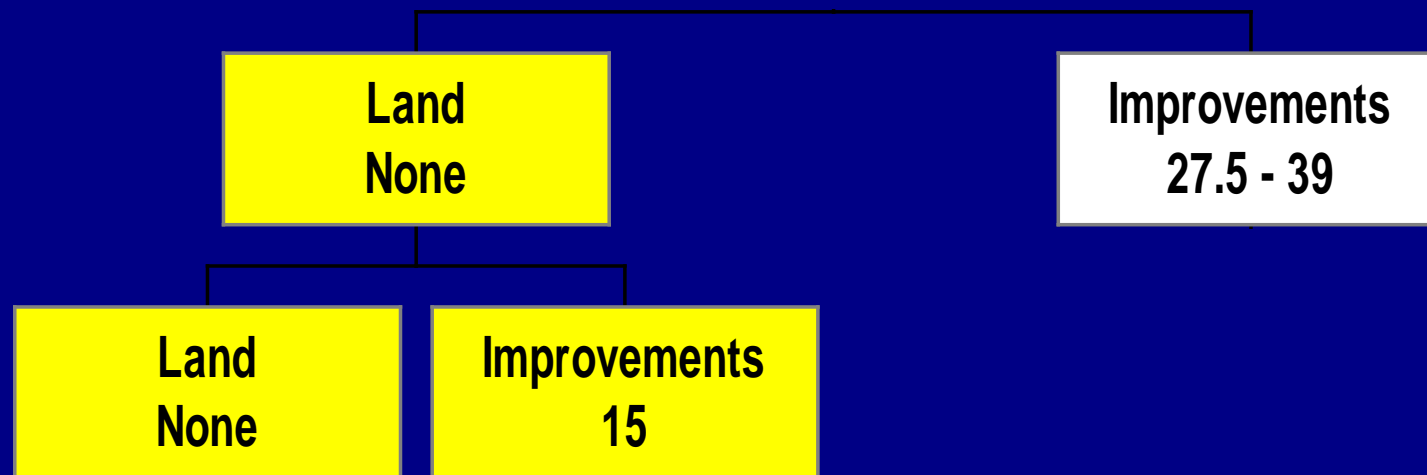
Filer	FY 2004	FY 2005	FY 2006
Form 1040 (by Income)			
\$ 0 – 24,999	1.25%	1.46%	1.49%
\$ 25,000 – 49,999	0.43%	0.60%	0.62%
\$ 50,000 – 99,000	0.44%	0.57%	0.62%
\$100,000 +	1.39%	1.41%	1.29%
\$1,000,000+	N/A	5.2%	N/A
Schedule C (by Gross Receipts)			
\$ 0 – 24,999	3.15%	3.88%	3.78%
\$ 25,000 – 99,000	1.47%	3.31%	2.09%
\$100,000 +	1.86%	3.85%	3.90%
S Corp (Form 1120S)	0.19%	0.30%	0.38%
LLC/Partnership (Form 1065)	0.26%	0.33%	0.35%

Make the Most of Depreciation

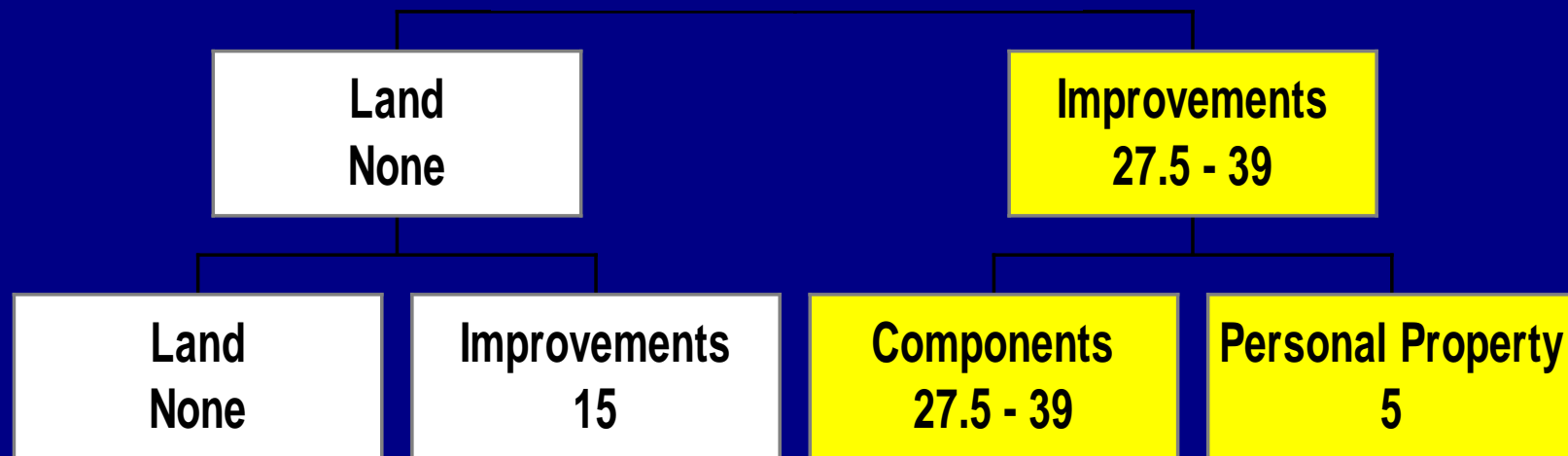


- Divide basis between “land” and “improvements.”
- Assign as much as possible to depreciable improvements.
- The IRS suggests you use local property tax assessments.
- You can use any allocation (such as bank appraisal or your insurer’s estimate of replacement costs) so long as you show “reasonable basis.”

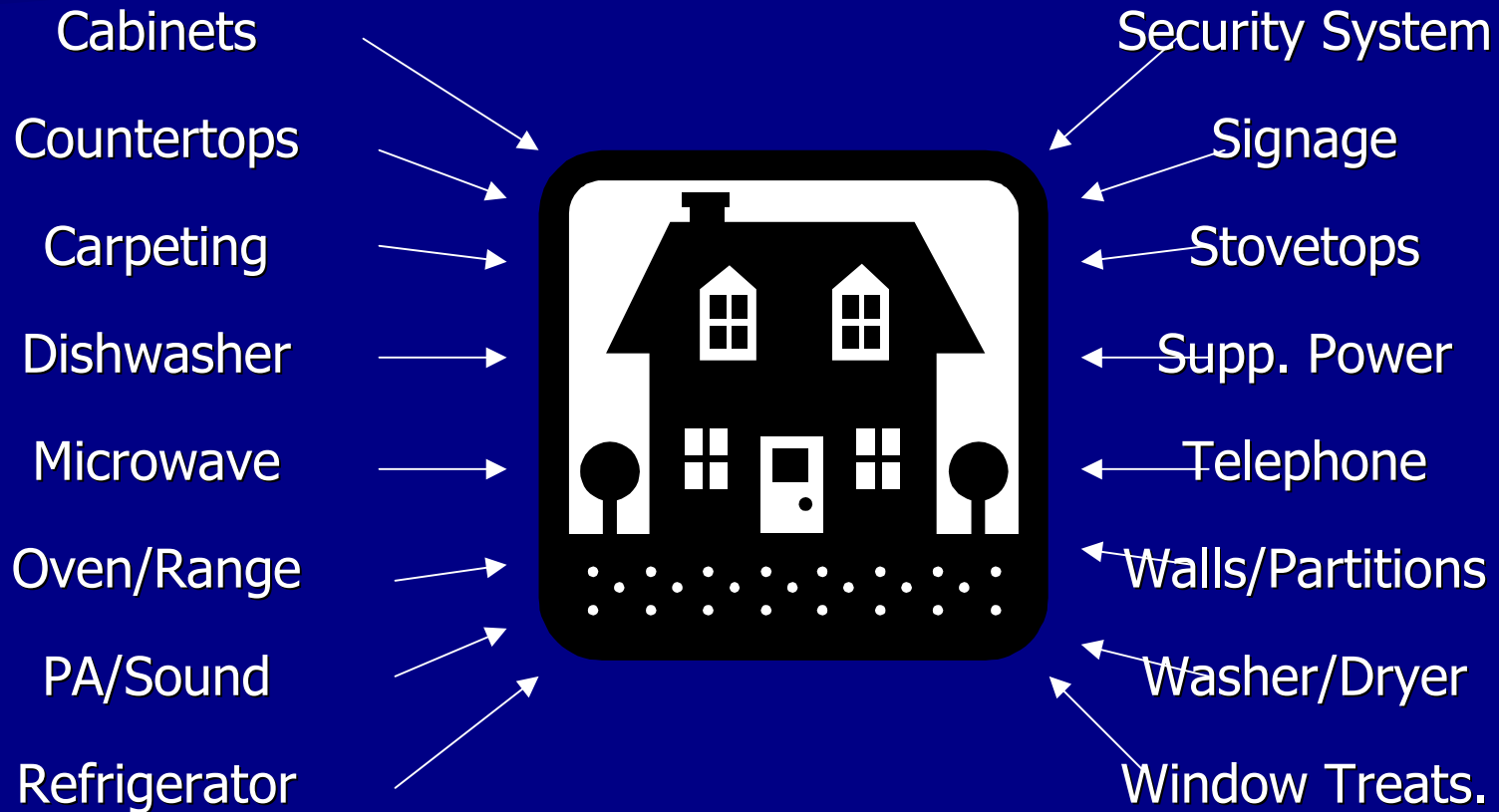
Break out Land Improvements



Break Out "Personal Property"



Personal Property Examples



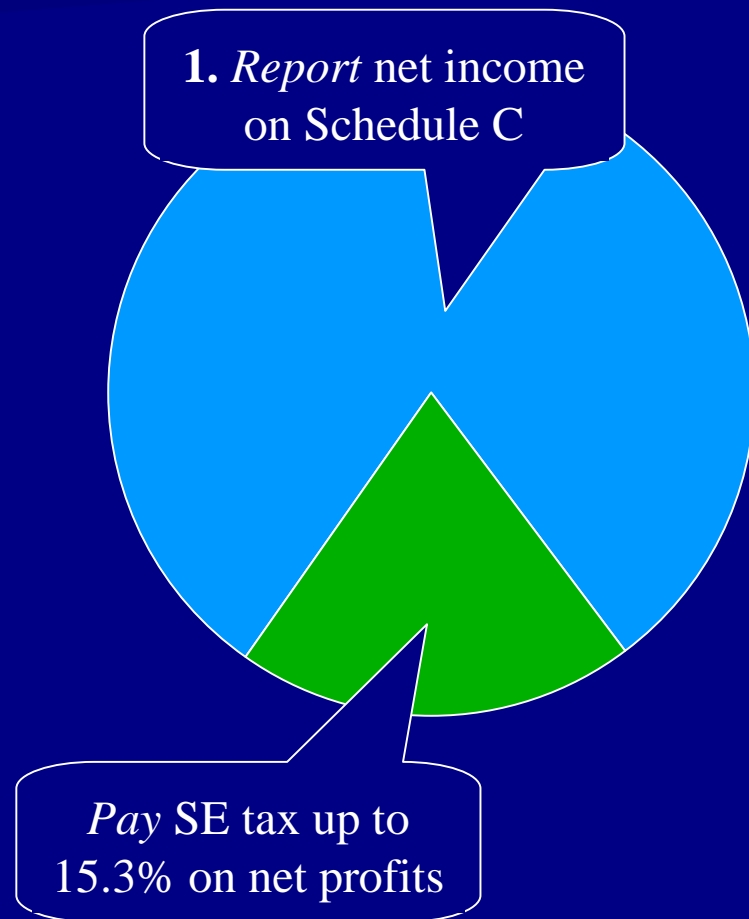
Repairs vs. Improvements

Repairs	Improvements
Deductible now	Depreciable over time
Keep property in good operating condition	Adapt property to new use
Don't add value	Add value to the property
Don't prolong property's use	Prolong the property's use
<ul style="list-style-type: none">■ Paint■ Plaster■ Repair broken windows■ Fix gutters, floors, leaks	<ul style="list-style-type: none">■ Room addition■ Upgrade appliances■ Landscaping■ Replace components

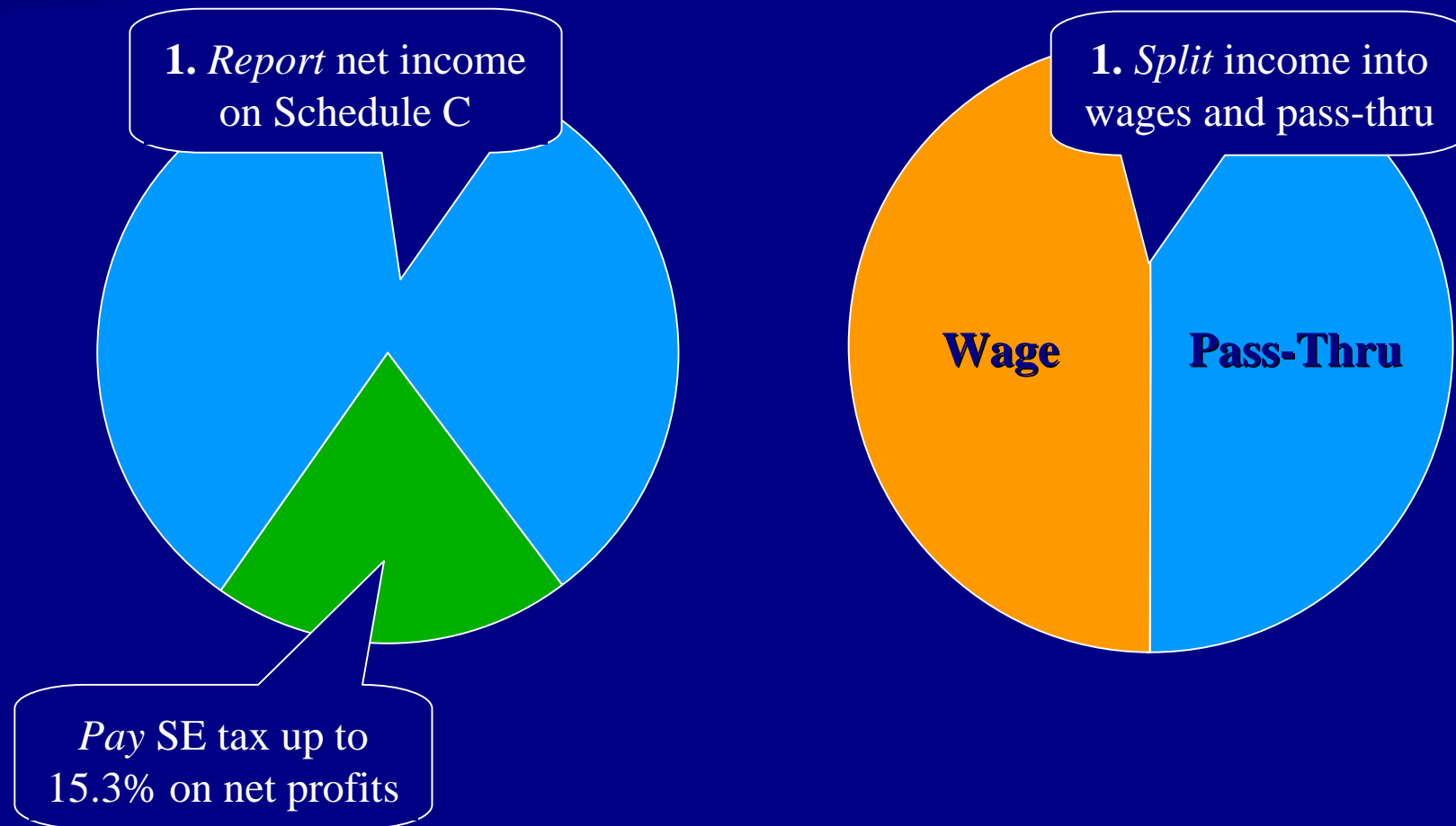
Investors vs. Dealers

Investors	Dealer
Buy as long-term investment	Buy with intent to resell in ordinary course of business
Avoid self-employment tax	Pay self-employment tax
Depreciation deductions	No depreciation deductions
Capital gains	Ordinary income
1031 Exchange	No 1031 exchange

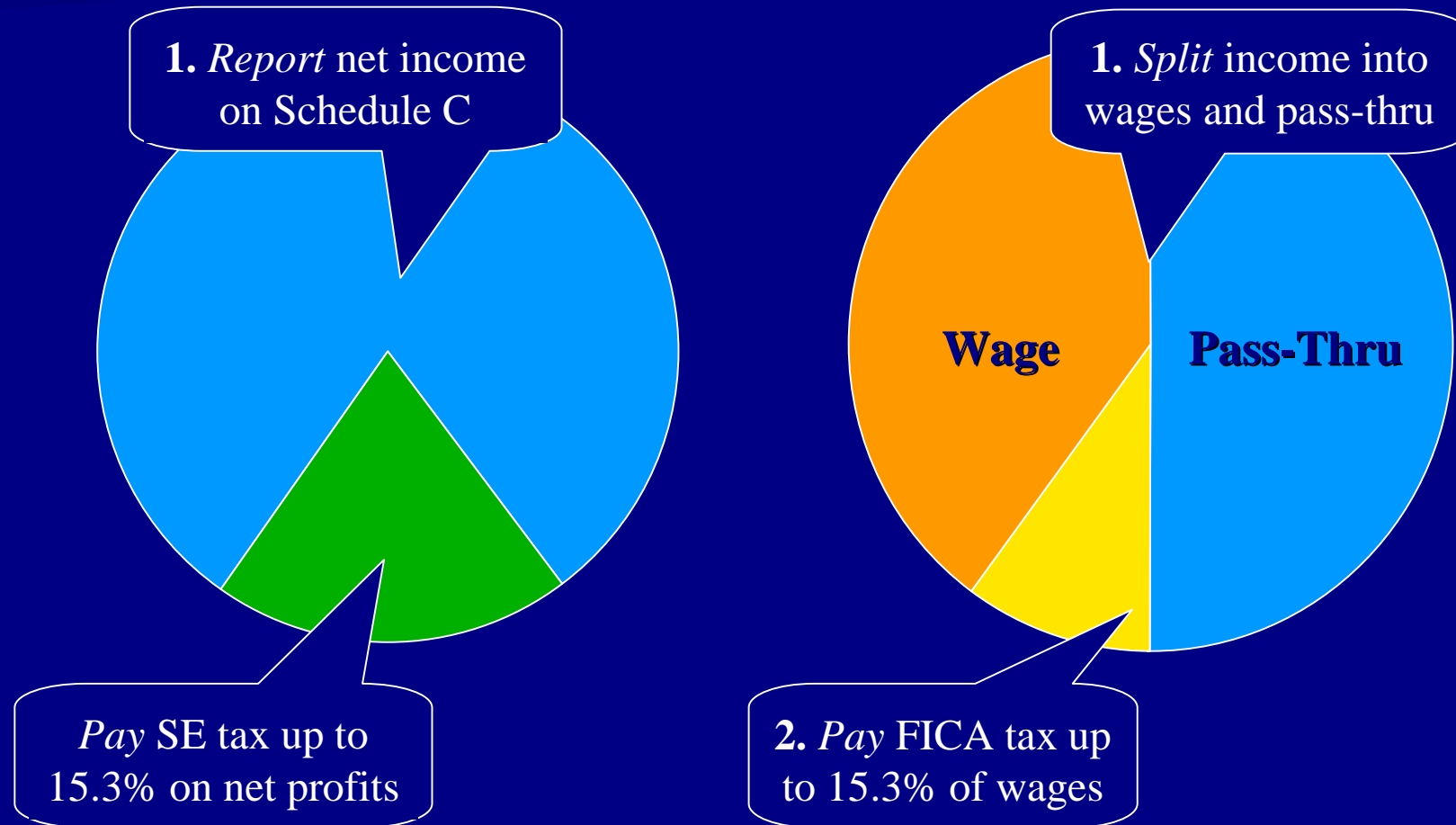
Cut Self-Employment Tax



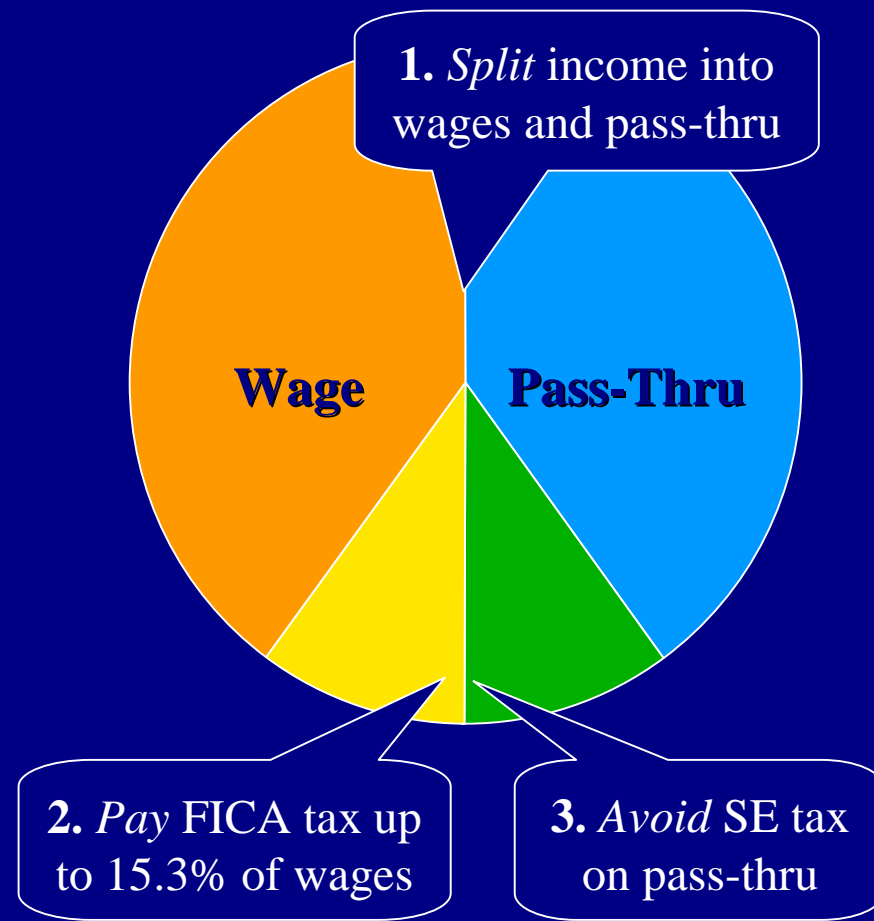
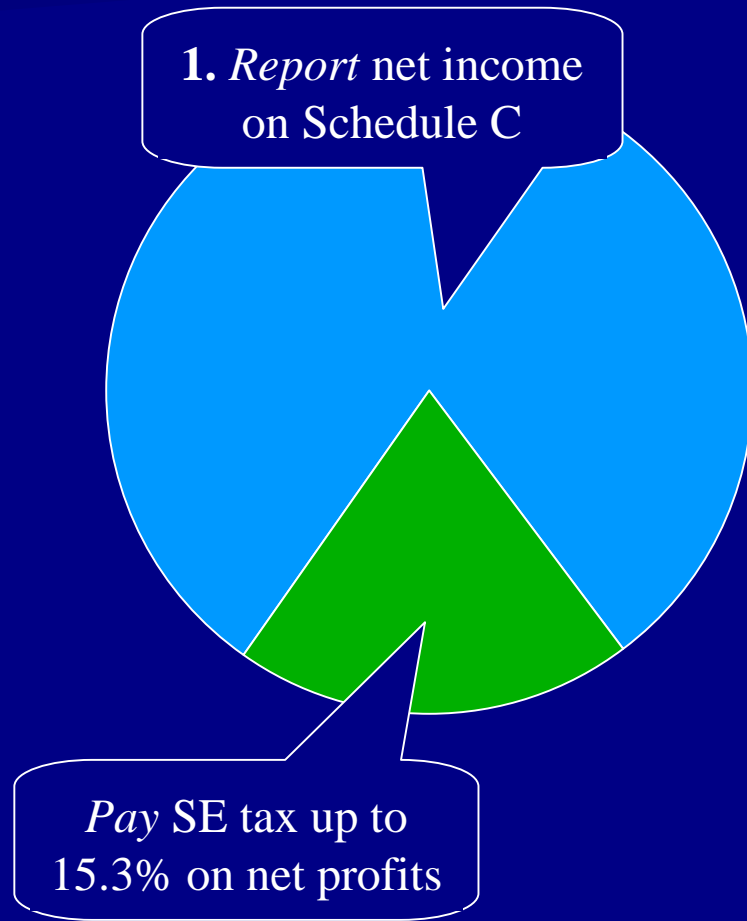
Proprietorship vs. S Corp



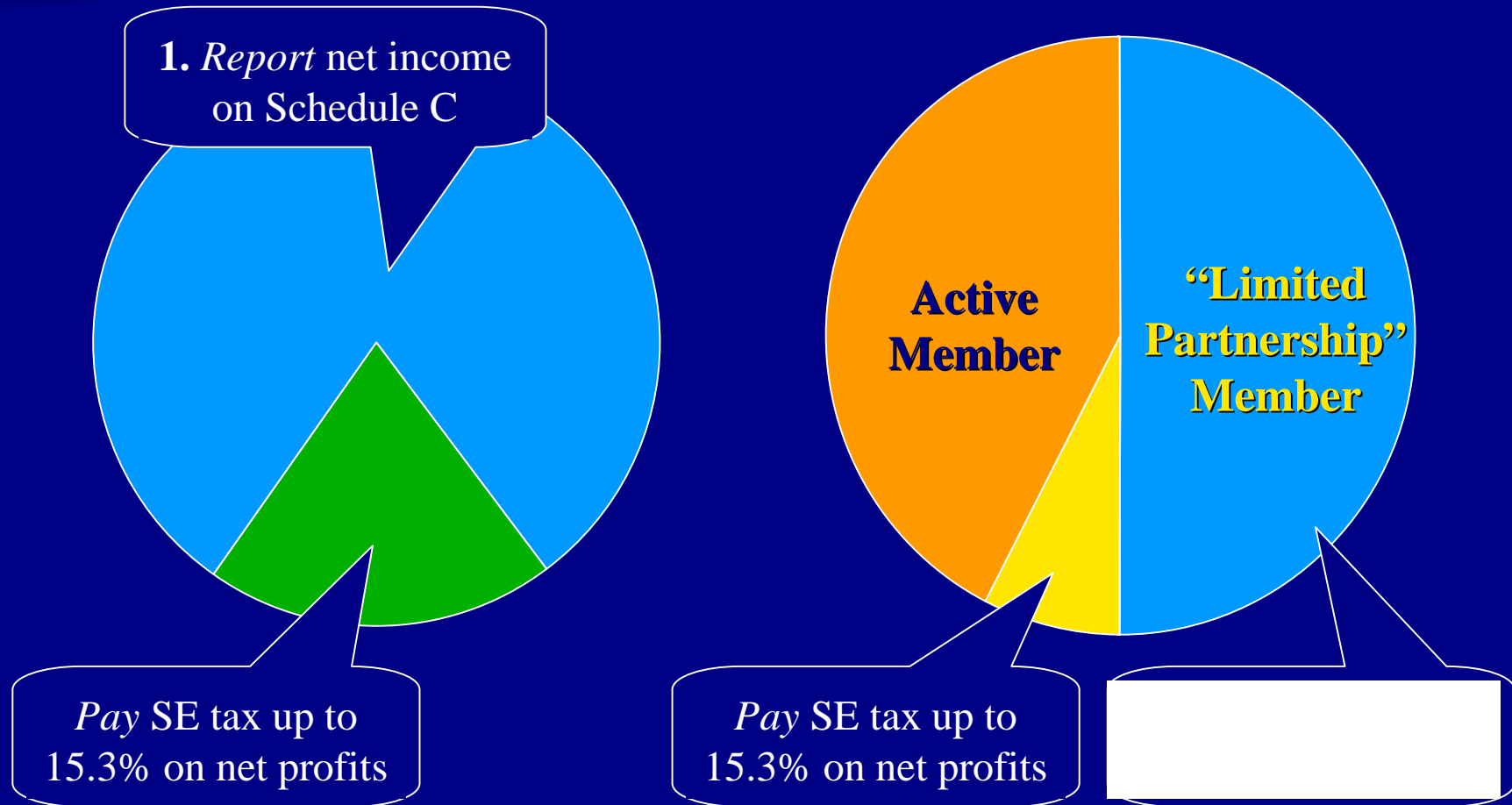
Proprietorship vs. S Corp



Proprietorship vs. S Corp



Proprietorship vs. LLC



Hire Your Family

- Children age 7+
- First \$5,450 tax-free
- Next \$8,025 taxed at 10%
- “Reasonable” wages
- Written job description, timesheet, check
- Account in child’s name
- FICA/FUTA savings

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Missing Medical Benefits

- Employee benefit plan
 - Married: Hire spouse (no salary necessary)
 - Not married: C-corp
- Reimburse *employee* for medical expenses incurred for self, spouse, and dependents
- Works with any insurance
 - Use your own insurance
 - Supplement spouse's coverage

MERP/105 Plan

- Major medical, LTC, Medicare, “Medigap”
- Co-pays, deductibles, prescriptions
- Dental, vision, and chiropractic
- Braces, fertility treatments, special schools
- Nonprescription medications and supplies

MERP/105 Plan

- Written plan document
- No pre-funding required
 - Reimburse employee
 - Pay provider directly
- Bypass 7.5% floor
- Minimize self-employment tax

Health Savings Account

1. “High deductible health plan”

- \$1,950+ deductible (individual coverage)
- \$3,850+ deductible (family coverage)

Plus

2. Tax-deductible “Health Savings Account”

- Contribute & deduct up to \$2,900/\$5,800 per year
- Account grows tax-free
- Tax-free withdrawals for qualified expenses

Example

Owner/spouse/2 children
25% federal/state tax
15.3% self-employment tax

Before

\$900/month premium

- no deductible/out-of-pocket
- \$15 co-pays
- \$10/\$20/\$40 drug card

\$10,800 *minimum*/year

- \$2,700 federal savings
- \$ 0 SE tax savings

\$ 8,100 after-tax cost

After

\$265/month premium

- \$5000 out-of-pocket max
- 80/20 drug co-pay
- 100% after o-o-p max

\$8,180 *maximum*/year

- \$2,045 federal tax savings
- \$1,156 SE tax savings

\$4,979 after-tax cost

Car/Truck Expenses

AAA Driving Costs Survey (2006)

Vehicle	Cents/Mile
Small Sedan	41.7
Medium Sedan	53.1
Large Sedan	61.9
4WD SUV	65.4
Minivan	59.2

Figures assume 15,000 miles/year; \$2.405/gallon gas

Missing Tax Coaching Service

- True Tax Planning
- Written Tax Plan
 - Family, Home, and Job
 - Business
 - Investments
- Review Returns