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Expiration of current capital gains tax rate would impact property owners taxes in 2013

July 26, 2012 - Spotlights

With the possible expiration of the current capital gains tax rate and the additional tax included in the health care reform legislation owners could see an almost 60% increase in taxes beginning in 2013. This is a result of the current capital gains tax automatically increasing from 15-20% if Congress allows it to expire. In addition beginning in 2013 the health care reform bill that became law in 2010 will impose an additional 3.8% 'Medicare tax' on non-wage income that would target high income earners, income from interest, dividends, capital gains, and some profits from investments in partnerships and S-corporations. If this tax and other tax increases included in the President's FY 2011 budget become law, certain taxpayers could expect a marginal tax rate on capital gains and qualified dividends of 23.8%. The possible 8.8% increase effectively results in an almost 60% increase from the previous tax of 15%.

The good news for owners thinking of taking advantage of the current low tax rates is the fact that the market has rebounded and this could be the most opportune time to sell since the last market peak. Due to the limited number of quality buildings available for sale, excessive demand by investors with access to historically low financing at rates of 4% or below, the multi-family market in certain areas is experiencing a boom. Since properties are purchased based on the net income the substantial rise in rents has increased bottom lines and in turn values.

Occupancy of multi-family properties in the Greater Boston market has increased dramatically resulting in little to no vacancies. New tenants entering the rental market include the recently foreclosed homeowner. During the last residential boom multi-family owners were losing tenants to homeownership with the result being higher vacancies. due to the loss of tenants to homeownership. Since the market crash the use of sub-prime loan programs are no longer available to first time buyers resulting in tenants staying put. Recent college graduates now gainfully employed are moving or staying in the city or areas where public transportation is available due to increased fuel costs. Many empty nesters are downsizing, selling their large suburban homes and testing the waters by renting first before buying. All of this has lead to a shortage in rentals resulting in rents rising substantially. For the first time in several years there are several developments being built for rental housing.

For owners who would like to sell and not pay the tax there is the option of deferring the gain through the use of the 1031 tax deferred exchange. A 1031 exchange allows you to sell investment property and defer the capital gains and depreciation recapture taxes, assuming reinvestment of 100% of equity into "like kind" property of equal or greater value. Any property held for investment purposes or for productive use in a trade or business generally qualifies as "like kind" property for 1031 exchange purposes. For the investors that want little to no management responsibilities there are alternative investments including the triple net lease and tenants in common (TIC).

A triple net lease is one where the tenant pays all of the ongoing operating expenses. The landlord receives a net rent, because the tenant pays the property taxes, utilities, insurance premiums, maintenance and repairs. Most net-leases are long term (10-25 years) with cost-of-living increases in the rent. Some examples of net-lease tenants are: Walgreens, CVS, Rite-Aid, and Barnes and Noble just to name a few.

An alternative to sole ownership of real estate is an investment in a single large commercial property by multiple owners, not as limited partners or as an entity, but as individual owners. Each owner receives an individual deed at closing for his or her undivided fractional interest in the entire property. This form of ownership is known as co-tenancy or TIC. Each owner has the same rights as would a single owner. A TIC replacement property enables the average investor to participate in an echelon of real estate previously reserved for large institutional investors.

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