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Expiration of current capital gains tax rate would impact property owners' taxes in 2012

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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 to 20% from 15% if Congress lets it just expire. In addition beginning in 2013 the health care reform bill that became law in 2010 will impose a new 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 in capital gains 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 financing at rates of 4% or below, the multi-family market is experiencing a boom. Since properties are purchased based on the net income the substantial rise in rents has increased the bottom line and values.

Occupancy of multi-family properties in the Greater Boston markets have increased dramatically with little to no vacancy. New tenants entering the rental market include the recently foreclosed homeowner. During the last residential boom multi-family owners were experiencing higher vacancy due to the loss of tenants to homeownership through the use of the now defunct sub-prime mortgages. Since the market crashed these 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 the increased cost of fuel. Many empty nesters are downsizing by 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 being driven up substantially. For the first time in several years there are several developments being proposed and on the table to be built for rental housing.

For owners who would like to sell but not pay the tax at all there is the option of deferring the gains 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. Besides purchasing a multi-family there is other choices for the investor that wants little to no management at all which include the triple net lease and the

Tenants-in-Common.

A triple net lease is one which 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 tenants-in-common (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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