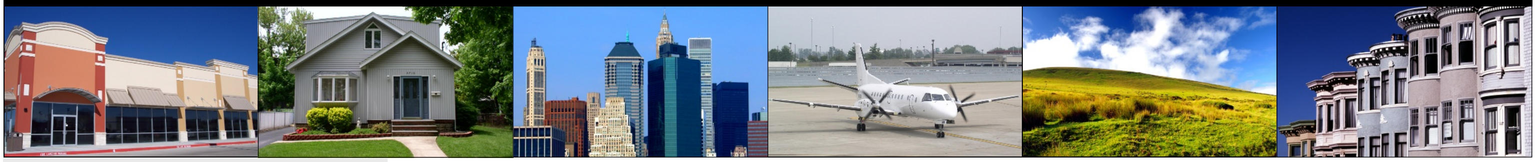
Tax Proposal Uncertainty Versus Tax Deferral Certainty with 1031 Exchanges



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Taxation, tax rates, tax deductions and overall tax fairness are certain to be dominant themes in a year with a presidential election in the fall. Many different tax proposals have been put forth by various committees and government representatives, but most believe that these proposals stand little chance of being enacted into tax law. Following is a brief overview of several different tax proposals.

TAX PLANNING UNCERTAINTY - RECENT TAX PROPOSALS

Bowles-Simpson Plan: The National Commission on Fiscal Responsibility and Reform released a report identifying ways to lower tax rates and eliminate some tax deductions. Their plan (often referred to as the Bowles-Simpson Plan) failed to get enough votes on December 3, 2011.

The Ryan Plan: The "Path to Prosperity: A Blueprint for American Renewal" is a budget proposal by Representative Paul Ryan, Chairman of the House Budget Committee. The Ryan plan lowers tax rates, eliminates some deductions, and reforms Medicare. It passed the House on April 15, 2012, but has little chance of being passed by the Senate.

The Buffet Rule: This plan (Senate Bill 2230) is named after investor Warren Buffet, and requires everyone making over $1 million a year to pay a minimum effective tax rate of at least thirty percent (30%). The plan's intent is to raise taxes on the rich and bring more "fairness" to the tax code. It failed to pass the Senate on April 16, 2012.

TAX PLANNING CERTAINTY - 1031 EXCHANGES

Tax strategies which take advantage of the current tax code are a much better way to achieve tax benefits today. IRC Section 1031 tax deferred exchanges have been a part of the tax code since 1921. Section 1031 allows an investor who holds property for business or investment to defer all capital gain taxes by exchanging the property for qualifying like-kind property under the rules and restrictions of Section 1031. By deferring the capital gain tax, an investor creates more purchasing power and better overall investment returns.

Let's compare the tax treatment for an investor holding investment property under the following scenarios: (i) selling the property in 2012; (ii) selling the property in 2013; and (iii) exchanging the property under Section 1031. We'll assume the property has $500,000 in capital gain, and $200,000 in depreciation recapture (taxed in both years at 25%). We will also assume a 15% capital gains tax in 2012, and a 20% capital gains tax in 2013 (as some people predict), plus an additional 3.8% Medicare surcharge for 2013 (as is also predicted for higher earners).

Sell in 2012; Pay Taxes:	$195,000 in taxes
Sell in 2013; Pay Taxes:	$239,000 in taxes
Exchange in 2012; Pay No Taxes:	$0 (no taxes owed)

By taking advantage of the tax deferral offered by Section 1031, the investor preserves net equity which is available to acquire better performing replacement properties. In times of economic and tax uncertainty, it is important to utilize the tax advantages currently available in the tax code. Call the experts at Asset Preservation to discuss 1031 exchanges and your investment property situation.

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