



DID YOU KNOW?

Did you know you can defer taxes on real estate gains using the 'lazy man's 1031'?

Section 1031 exchanges are a powerful tool for deferring tax on the sale of business or investment real estate. Unfortunately, its requirements are fairly technical and the timing restrictions are unforgiving. In order to defer gain, the sale proceeds must be reinvested in another property which is identified within 45 days and acquired within 180 days of sale of the property. Obviously, it can be very challenging to identify and close on a new property within these time periods.

A more forgiving alternative can be to invest in a real estate investment syndication (a.k.a. partnership). The sponsor of the syndication (also known as the general partner or operator) will typically perform a cost segregation study with respect to the property the partnership acquires which allows it to maximize the bonus depreciation deductions (currently 100%) the partnership can take. These depreciation deductions translate into losses which are allocated to the partners in the first year and can range in amount from 30% to 80% of the amount of the partner's investment.

For example, assume an investor sold a property with a \$100,000 tax basis for \$180,000 and invested the entire amount into a syndication. Assume further that partner's share of losses for the year is \$90,000. That loss will entirely offset the sale gain of \$80,000 plus \$10,000 of income that the partner may be subsequently allocated for the syndication.

Unlike a section 1031 exchange, this method is effective as long as the sale and purchase occur within the same tax year. The 100% bonus depreciation that helps to generate the loss to offset the sale gain begins to phase out next year (20% per year), so the utility of this method may decrease over time, but may nevertheless provide substantial relief when a 1031 exchange is impractical.

Bottom Line: When a Section 1031 Exchange is impractical, you may want to consider investing in a real estate partnership and offset the sale gain using losses from accelerated depreciation.

"Change is not a four letter word...but often your reaction to it is!" – Jeffrey Gitomer



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