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TAXES

The Tax Blotter – Jan. 20, 2023

The tax law provides generous tax breaks to investors in real estate, but there are several key tax pitfalls to watch out for.

Ken Berry • Jan. 19, 2023

The Tax Blotter is a round-up of recent tax news.

The tax law provides generous tax breaks to investors in real estate, but there are several key tax pitfalls to watch out for.

Be more active. Generally, deductions resulting from passive activities are limited to the income received from passive activities, so you can't write off a current loss. Real estate is automatically treated as a passive activity. However, you can use up to $25,000 of loss to offset non-passive income if you are an active participant in a real estate activity. The $25,000 real estate loss offset is phased out for a modified adjusted gross income (MAGI) between $100,000 and $150,000 of MAGI.

Swap in time. If you sell investment real estate, you generally have to pay capital gains tax, up to maximum rate of 20% on long-term capital gain. But you can defer tax indefinitely by exchanging the property for other like-kind real estate. The Tax Cuts and Jobs Act (TCJA) eliminated this tax break for like-kind exchanges, but preserved it for real estate. Caveat: You must (1) identify the replacement property within 45 days of the transfer and (2) receive title to the replacement property within the earlier of 180 days or your tax return due date, plus extensions,

Are you a pro? The passive activity loss (PAL) rules generally prevent you from deducting losses from real estate activities. But there's no such restriction if you qualify as a real estate professional. Notably you must spend at least half of your personal services time on real estate and log in more than 750 hours at the activity. New case: A couple reported substantial real estate losses but neither could establish from records that they individually satisfied either part of the tax law test. Accordingly, the losses were denied (Dunn, TC Memo 2022-112, 11/29/22).

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