Tax Rates for 2013 and Tax Planning for Sale of Real Estate

The American Taxpayer Relief Act of 2012 was enacted in the early morning hours of January 1, 2013 and establishes the new rules for capital gains tax rates and other taxes on the sale of real estate.

Capital gains on the sale of assets held more than 12 months are taxed at a lower rate than ordinary income. The Jobs and Growth Tax Relief Reconciliation Act of 2003 and Tax Reconciliation Act of 2006 temporarily reduced the tax rate on long-term capital gains until January 1, 2011. Congress extended the reduced tax rate until January 1, 2013. At this time, the previous rates are scheduled to be automatically reinstated unless Congress once again extends the reduced rates.

As a result, taxpayers face uncertainty about whether they should be planning for taxable gains in 2012 or 2013. Or, whether they should defer their taxes under Code Section 1031 with an exchange of real estate or cash-out and take their gains in 2012 before a higher tax rate becomes effective.

Tax rates on long-term capital gains on a sale of real estate now and in 2013 can be summarized as follows if there is no further action by Congress –

Now	2013	
15%	20%	Taxpayers in a regular tax bracket higher than 15%
0%	10%	Taxpayers in the 15% or 10% regular tax bracket

Capital gains (long-term) attributable to depreciation taken on real estate investments are taxed at a rate of 25% (15% for taxpayers in a 10% or 15% tax bracket) before the above referenced tax rates begin to apply.

Commencing in 2013, a new Medicare tax of 3.8% will be imposed on capital gains from the sale of real estate for high-income taxpayers. High-income taxpayers are taxpayers with gross income of $200,000 for individuals or $250,000 for couples. This tax will only apply to the amount of gain which causes adjusted gross income to exceed the high-income threshold. Real estate used in a trade or business will not be subject to this tax. Real estate sold by a Real Estate Professional also will not be subject to this tax. A Real Estate Professional is a taxpayer who spends more than half of his time during the year (and at least 750 hours of service) in real property trades or businesses in which he materially participates.

Talk to your tax advisor about your alternatives in this uncertain tax environment. You may find that a 1031 Exchange remains desirable as an alternative to paying taxes under either rate schedule. Call us at 888-367-1031 or email us at 1031@1031cpas.com if we can help with any questions. Our Exchange Manual is also available free of charge at www.1031cpas.com. 1031 Corporation is the Intermediary of choice for real estate professionals, CPAs and investors.

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