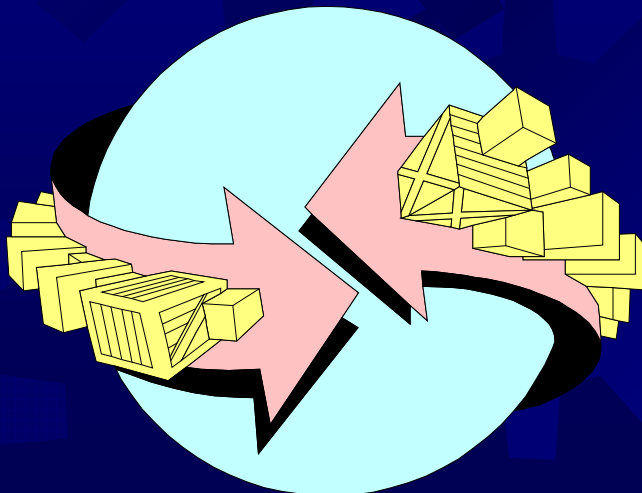
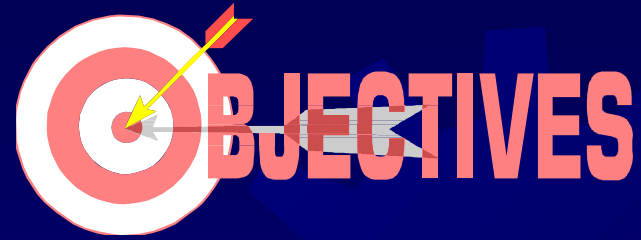


CHAPTER FOURTEEN

REAL ESTATE TAXATION AND EXCHANGING



Chapter 14



1. Understand the concept of basis
2. Calculate property taxes and pro-rations
3. Discuss various state propositions
4. List the various tax exemptions
5. Describe the requirements for an installment sale
6. Name the licensee's responsibilities and obligations.

TERMS

- ★ **Original Cost BASIS**: Dollar amount assigned to property at time of acquisition under provisions of the Internal Revenue Code for purpose of determining gain.
- ★ **Adjusted Basis**: Cost basis after additions for improvements and subtraction for depreciation.
- ★ **GAIN**: Profit, benefit or value increase. (versus actual **CASH REALIZED** from the sale.)
- ★ **Internal Revenue Code (IRC)1031 Exchange**: Tax-deferred exchange of like-kind properties held for investment or business uses.

BASIS – Investment Property

Purchase Price \$100,000

(Original Basis)

★ Improvements + 25,000

★ Depreciation - 50,000

★ Adjusted Basis ~~\$75,000~~

\$75,000

★ Sales Price \$200,000

★ Cost of Sale -25,000

★ Net Sales Price \$175,000

★ Adjusted Basis \$75,000

● Gain from Sale \$100,000



Basis with Loans – Investment Property

Purchase Price	\$100,000
(Original Basis)	
★ Cash Investment	20,000
★ Original Loan	<u>80,000</u>
★ Improvements	+ 25,000
★ Depreciation	- 50,000
★ Adjusted Basis	<u>\$75,000</u>
★ New Loan (Refi)	\$150,000
★ Sales Price	\$200,000
★ Cost of Sale	<u>-25,000</u>
★ Net Sales Price	\$175,000
★ Adjusted Basis	<u>\$75,000</u>
● Gain from Sale	<u>\$100,000</u>
● Cash From Sale	<u>\$25,000</u>

\$75,000



“Equity over basis”

Cash realized is less than taxes owed!!

Taxes owed greater than cash realized!!

Property Tax, pro-ration Information

- ★ fiscal Year: July 1 – June 30
- ★ Reassessment upon recordation - Proposition 13
- ★ supplemental tax bill will be drawn for prorated portion due for balance of current tax year
- ★ Tax installments are due **Nov 1** and **Feb 1**
- ★ Tax installments delinquent **Dec 10** and **April 10**

No
Darn
Fooling
ARound

Prorations

- Prorations may be based on:

30 days in each month

360 days in each year

Items frequently prorated include:

I nterest

T axes (property)

A ssociation dues

R ents

PROPOSITION 13

- ✦ Property taxes are limited to 1% of full cash value + any special assessments
- ✦ Taxes may only be increased 2% each year
- ✦ Property is reassessed upon transfer or completion of new construction



Tax Propositions

No change in property taxes/No reassessment:

- ★ Proposition 58: Between spouses, parent & child, child & parent.
- ★ Proposition 60: Same county (age 55+)
- ★ Proposition 90: Different county within California.

Real Property Tax Exemptions

- ★ Nonprofit Charitable Organizations
- ★ Churches
- ★ Government Agencies
- ★ Nonprofit Educational Institutions
- ★ homeowners
- ★ Veterans
- ★ Senior Citizen Tax Postponement
- ★ Renter's Relief Provision

Tax Deduction Advantages Income Property

- ☀ interest expense on Real Estate loans
- ☀ property taxes & assessments paid
- ☀ Maintenance & operating expenses
- ☀ Depreciation deductions allowed
- ☀ Long-term capital gains on residence resale
 - Up to \$250,000 for taxpayer filing singly
 - Up to \$500,000 for married couple
- ☀ installment sales to postpone tax on gain
- ☀ Taxes deferred in exchanges
- ☀ Tax deferment under certain circumstances
- ☀ Tax savings through sale and leaseback

New IRS *SHORT* Form

Line 1 How much did you make? \$ _____

Line 2 Send it in. \$ _____

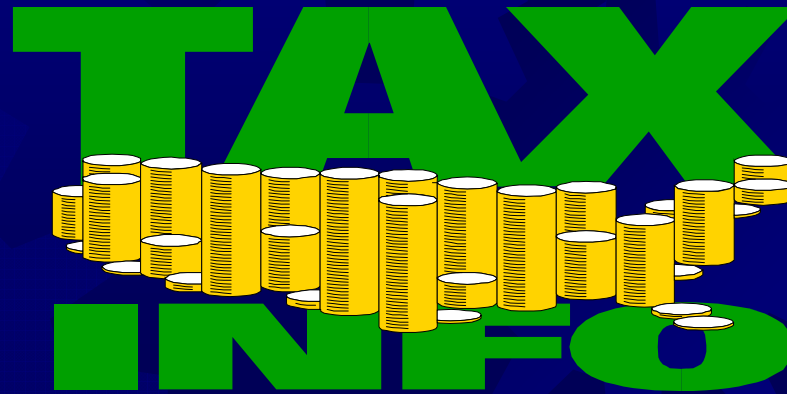
• Signature _____ Date ____ / ____ / ____

Tax "FREEDOM" Day

★ 1950	April 3 rd	80%
★ 1972	April 28 th	70%
★ 1985	April 19 th	50%
★ 1993	May 3 rd	31%
★ 1994	May 12 th	39.6%

Installment Sale

- ☀ Income tax not due until the profit is actually received on the gain.
- ☀ Owner/seller carry back loan.
- ☀ Interest income is always taxed.



Tax-Deferred Exchange Rules

- ✦ Investment or business property
- ✦ Uses the IRC 1031 exchange rule
- ✦ Like-kind Rule



DRE Licensee's Role

“WE ARE LICENSED IN CALIFORNIA TO SELL REAL ESTATE, NOT TO GIVE LEGAL OR TAX ADVICE!”

Recommend that client get a legal or tax Counselor/Advisor.

Stay current and Avoid structuring obvious pitfalls.

Pg 143-144

