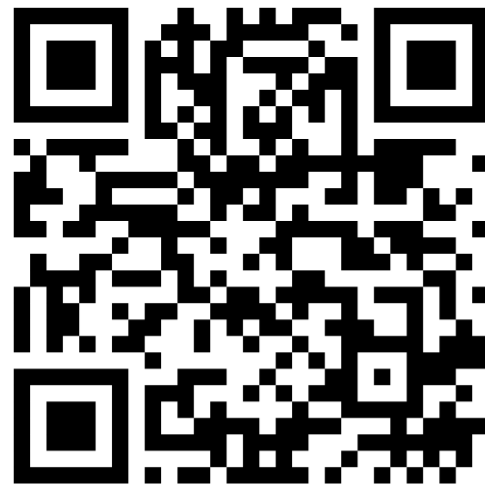


Real Estate Tax Hacks: Write-offs for Realtors

Scan for my contact info:



Digital Handout:



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Intro Video



Before We Dive In



- Eliminate Distractions
- Keep questions general
 - We'll be happy to take detailed, personal questions by appointment
- Please avoid political questions/comments
- Please provide Feedback

Course Objectives

- Understand the value of legally taking advantage of tax laws and penalties for errors (intentional or not)
- Why and how to avoid an IRS Audit and how to choose a great tax pro
- Entity selection – Sole Proprietor, LLC, Partnership, S-Corp, etc.
- Deductions and credits – walking the line
- What to keep track of and what documents to keep
- Huge advantages for real estate investors
- Tax strategy with reverse mortgages
- Qualifying for a mortgage while self-employed



Why Are Taxes Such a Hot Topic?

- W-2 employees don't experience having the money before being required to give it to the IRS
- Self-employment taxes are higher if you don't have it optimally set up
- TikTok tax influencers make it seem like nobody pays taxes



Common Audit Triggers for Realtors

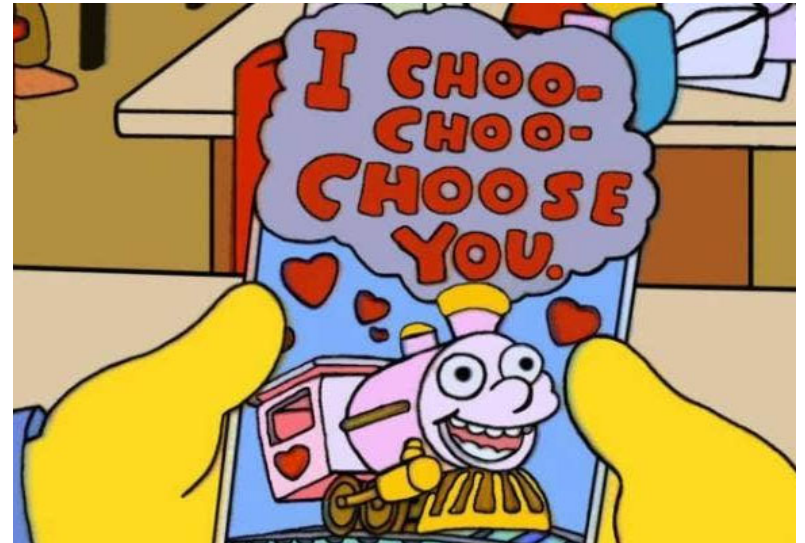
- Not reporting income that another entity reports
 - Examples - employer reports your income but you do not, an entity issues a 1099 to you and you don't report it
 - Entities report your income to demonstrate a legitimate expense for themselves
- Significant inconsistencies and bucking standards
 - IRS has a good idea what acceptable profit margin ranges are for all established industries/professions
 - Wildly fluctuating expense ratios over several years
- Use lots of round numbers
- High travel, mileage, meals expenses

Other Audit Triggers

- Net Operating Losses (NOLs), especially for non-corporations
- Self-employment
- Heavy use of tax credits
- Claiming specialized statuses
- S Corps not doing payroll

How to Choose a Tax Pro

- Interview
 - What do you specialize in?
 - How do you communicate with your clients?
 - What are your typical response times?
- Red Flags
 - No credentials
 - Refund loans
 - Not signing a return
 - Refund-based fees

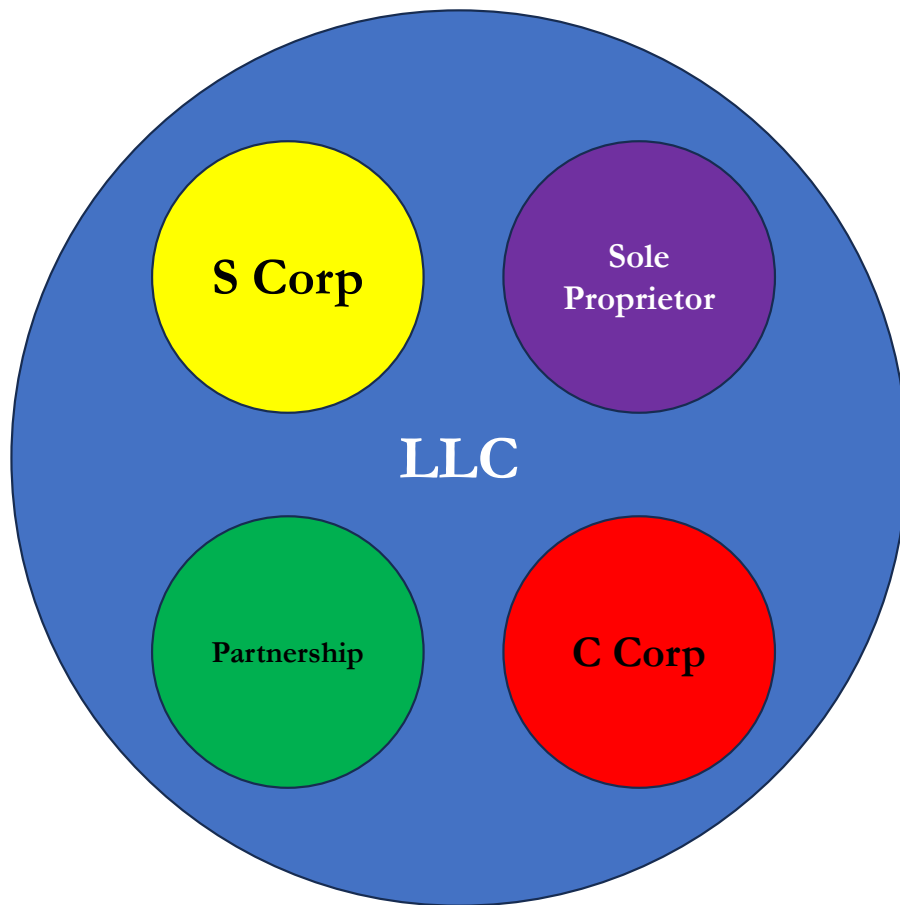


Who is Responsible?

- Your tax preparer is **NOT** an auditor!
- They should provide guidance, but ultimately the most important signature on the return is **YOURS**
- They probably won't be going into your revenues, expenses, or receipts line by line



Tax Entity Selection Options



- It's not LLC or S Corp
- LLC/PLLC filing as a:
 - Sole Proprietorship
 - S Corp
 - Partnership
 - C Corp

Business Bank Accounts

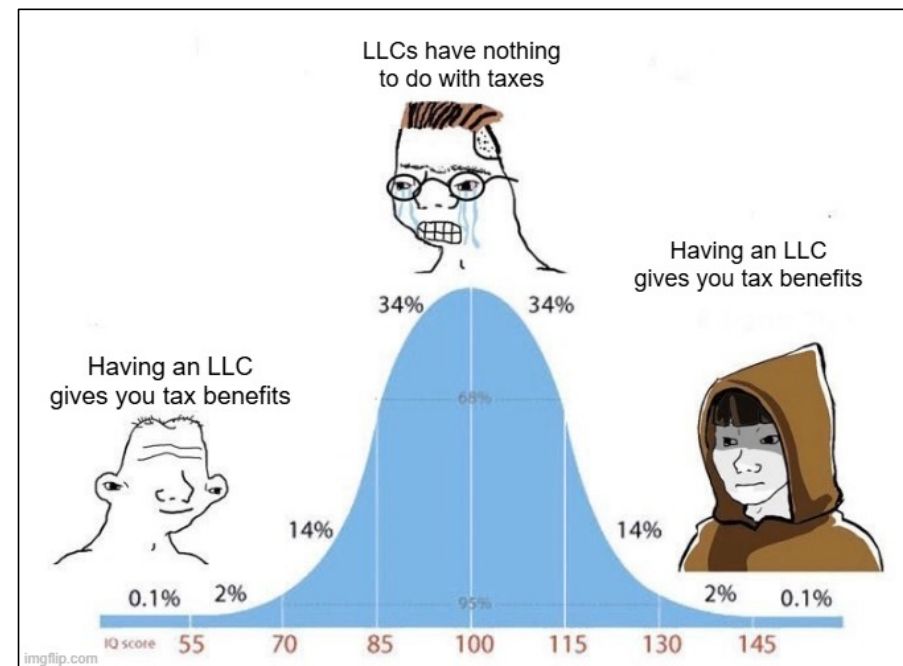


Why you should get a business bank account:

- Legal protection
- Clear financial separation
- Makes bookkeeping WAY easier!

Entity Selection – LLC

- Limited Liability Company
 - Protects personal assets from business liability
 - Business structure recognized by state statute
 - Some types of businesses are not allowed be LLCs (banks, insurance companies)
- Default tax structure
 - Single member – Sole Proprietorship
 - Multiple members – Partnership
 - Can elect to be taxed as a different classification, such as an S-Corp



Entity Selection – Sole Proprietorship



- Sole Proprietorship – default
 - Okay for net profits up to ~\$40k-50k
 - Biggest difference between this and other entities: self-employment taxes
 - No requirement to have an LLC, although it's a good idea to have one

How Self-Employment Taxes Work



BOSS
BABE

- For all W-2 wage earners, Federal Insurance Contributions Act (FICA) taxes are due equal to 15.3% of W-2 wages, including bonuses
 - Employers and employees each pay half (7.65%)
 - Self-employed taxpayers pay all 15.3% themselves
- Only income up to \$184,500 (2026) is subject to Social Security taxes

Entity Selection – S-Corp

- S-Corp
 - Income taxes pass through to the owners; the entity itself isn't taxed
 - Employment taxes are still due, but only on “reasonable salary” portion
 - 20-50% of net profit can be posted as wages
 - S-Corp election great when NET PROFITS = ~\$40-50k+
 - S Corp calculator ([link](#))
 - Much lower chance of an audit!



S-Corp Election is a Long-term Decision!



- Making the S Election should *not* be based only on current year tax savings!
- Admin/accounting/payroll costs
- More financial discipline
- If you revoke it, you can't have it back for 5 years
 - Can't just start a new LLC and make a new election next year
- Lower Social Security checks in retirement – invest the tax savings

Entity Selection - Partnerships

- Partnerships
 - Taxes are “passed-through” just like an S-Corp
 - Best for multi-owner rental properties
 - Active partners pay self-employment taxes on their allocation of the profits
 - DON'T put a passive spouse in an active business like RE sales!



S-Corp vs Partnership



- S-Corp best for RE agents when $> \$50k$ net profits
- Passive (investor, usually) partners in a partnership can avoid SE taxes
- S-Corps for RE investing:
 - Great for fix and flip
 - **BAD** for holding investment properties! Capital gains minefield!

Deductions vs Credits

Deductions (Write-offs)

- Reduce taxable **income**
- Reduce taxes by marginal tax %

Example:

Eligible business expense of \$1,000

Marginal tax rate of 22%

Taxes owed reduced by **\$220**

Credits

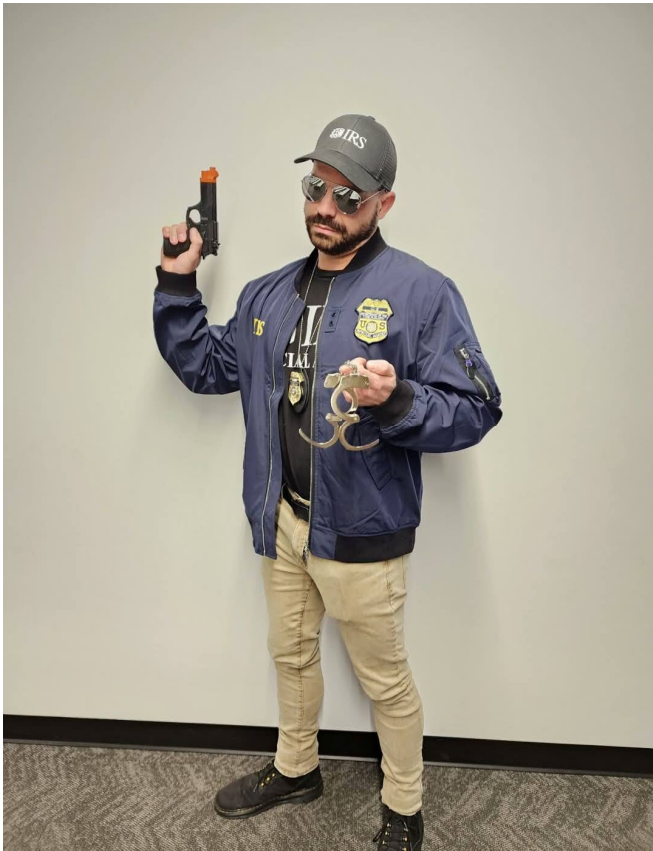
- **Directly** reduce or refund tax dollars
- 1:1 ratio

Example:

Eligible child tax credit of \$1,000

Taxes owed reduced by **\$1,000**

Deductions

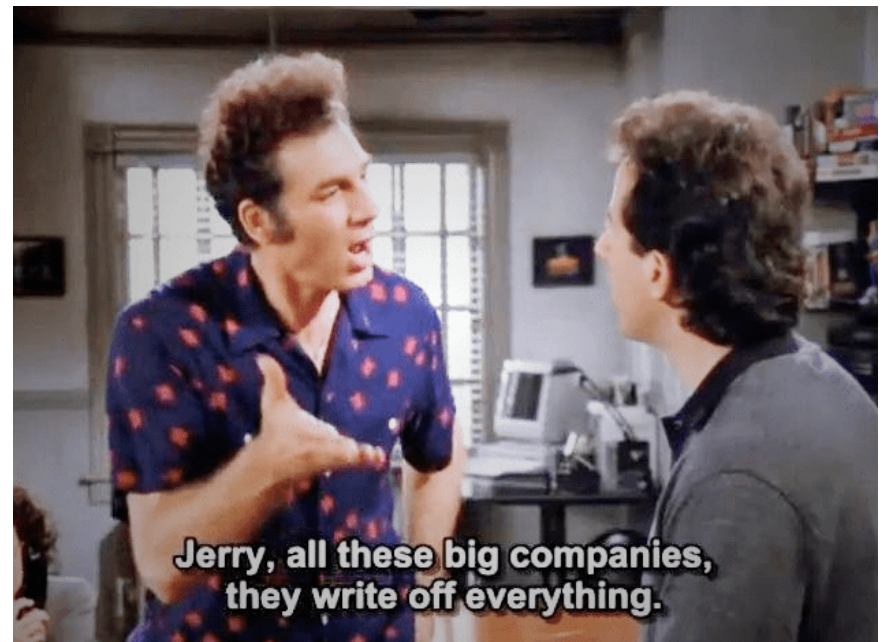


Pro Tip:
It's not how *you* justify a deduction to the IRS, it's how the IRS *allows* you to justify it.

Deductions

Business Expenses

- “Costs incurred in the ordinary course of business”, “specific, **EXCLUSIVE** business use”
- Marketing – signs, advertisements, swag, social media ads, etc.
- Bookkeeping, accounting, tax prep
- Professional memberships, courses, seminars
- Cell phone bill



Deductions – Home Office



Home Office

- Based on square footage of your home
- Two ways to calculate it, but leave the math to your tax preparer.
- Must be used only for business

Deductions – Vehicle and Mileage

Vehicle

- Either mileage OR actual expenses
- Mileage is often better for business loan or mortgage qualification
 - Easy to track with apps such as MileIQ
- Expenses (percentage):
 - Depreciation (cost of vehicle over several years)
 - Gas
 - Repairs/maintenance
 - Car washes/detailing
- Business purpose parking and tolls, NOT tickets
- Interest is deductible either way
- 6k lb. rule – may greatly accelerate depreciation in year 1



Deductions – Travel



Travel

- Conferences, trainings, client meetings
- 4 hour/day rule
- Airline tickets, meals (50%), lodging
- NOT entertainment (sports tickets, movie tickets, golf)
- Vacation days before/after should be excluded

Deductions – Meals

Meals – 50%

- Rule of thumb – if not traveling, eat with someone
- Not considered “lavish or extravagant”
- Meals to network with prospects, clients, and referral partners are deductible
- Make quick note on receipts (with whom, why)



Deductions – Retirement Contributions



Retirement Contributions

- 401(k), Solo 401(k), SEP, IRA
- This *defers* taxes; does not eliminate them!
- I prefer Solo 401(k)s to other vehicles for RE agents

Deductions – Health Savings Accounts



Health Savings Accounts (HSAs)

- Avoids taxes entirely for funds used for qualified medical expenses – income-reducing expense AND not taxed when distributed
- Must have a high-deductible health plan
- Max contribution \$4,400 if single, \$8,750 for family in 2026

Deductions – Hiring Your Kids Under 18

- Deduct what you pay them
 - If <18 years old and pay is under \$16,100 they don't need W-2s or 1099s
- Help pay for their extracurriculars and hobbies
- Teaches responsibility!
 - Value of work and money
 - Time cards
 - Roth IRA



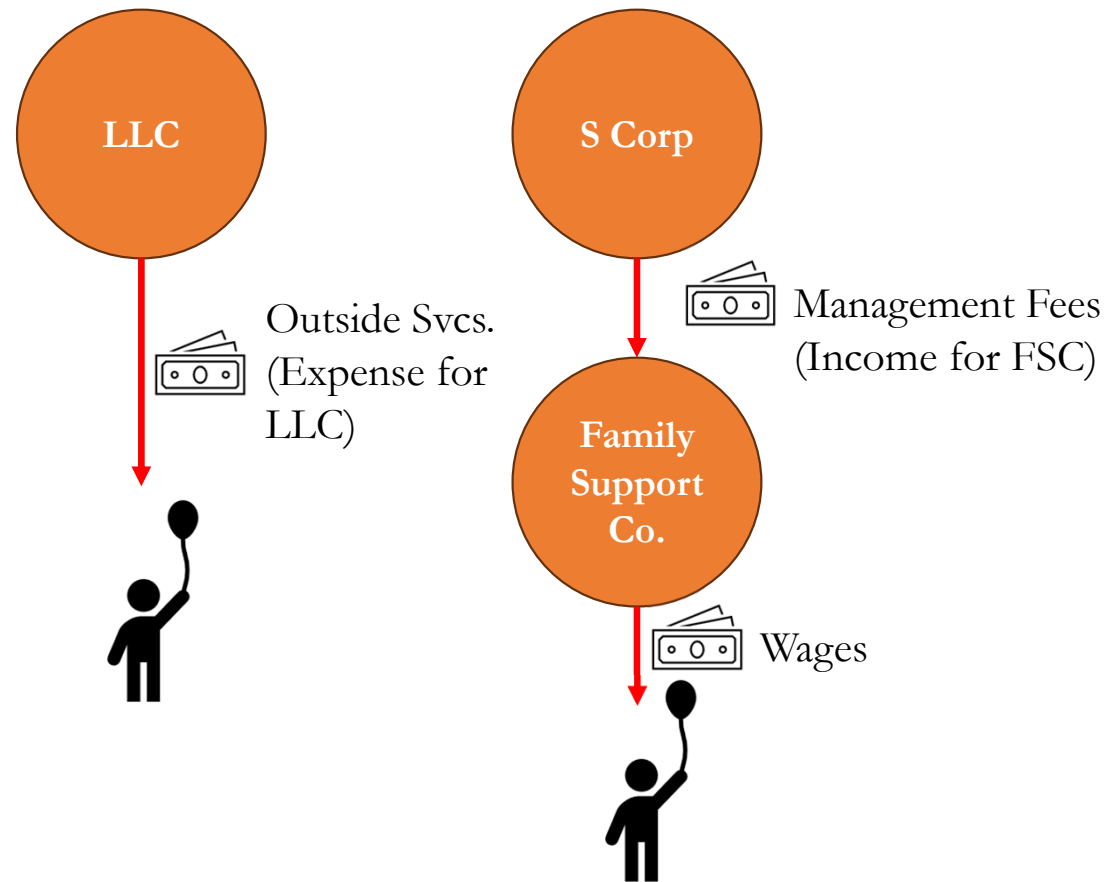
Deductions – Hiring Your Kids Under 18

- You can hire your kids to do legitimate, age-appropriate tasks for your business
 - Janitorial
 - Videography/social media
 - Creating and sending flyers/mailers
 - Event/open house assistance
 - Staging
 - CRM Maintenance



Deductions – Hiring Your Kids Under 18

- Sole Prop or REI LLC – Record as Outside Labor
- S Corps must use a Family Support Company (doesn't need to be an LLC), which would be its own zeroed-out company



Deductions – Hiring Your Kids 18+



- No need for FSC for S Corps
- Must issue a W-2 or 1099
- Kids should file a tax return
- Add them to Board of Directors/Advisors
- Starts building a financial profile
- Cheaper health insurance than being on yours

Deductions – Strategic SALT Payments



- If you are filing as an S Corp or Partnership, you can make a strategic State and Local Tax (SALT) payment near the end of the year. This will allow you to write off the payment as a business expense instead of needing to rely on itemizing your deductions to deduct your state taxes.

Deductions – Strategic SALT Payments

- In many states (including Utah) you can have your S Corp or Partnership pay your state taxes for you (usually not REI LLCs)
- Legally write it off as a business expense
- Don't have to rely on itemizing deductions to take advantage



Can I Deduct It?

- Clothing with your logo
- Client appreciation events (ent.?)
- Makeovers
- Groceries for your family
- Restaurant Food
- Charitable Contributions
- Personal miles driven in a car with your logo on it (marketing?)
- Cell phone bill
- Utilities
- Concert tickets for prospective clients or employees



Credits



- Not a lot of federal tax credits available for single person businesses for most kinds of businesses
- Personal credits
 - Child and Dependent Care Credits
 - Education Credits

Quarterly Payments

- As a business owner, you need to send quarterly payments to the IRS – penalties if you don't – 0.5% of amount unpaid each month
- Due April, June, Sept, and Jan 15th
- Based on prior year income or current year estimates – ask your tax preparer to help you
- Rules are slightly different if you make >\$150,000
- Easily paid online at irs.gov/payments



What to keep track of

- Business expense receipts
- Business bank account
- Mileage – MileIQ, Quickbooks
- Auto expenses
- Home office sq footage
- Cell phone bill
- Internet bill
- Meals – write notes on back of receipts
- Quarterly payments



Capital Gains

You incur a (normally) taxable gain when you sell an asset for a higher price than your basis.

Capital Gain = Sale Price – (Basis + Selling Expenses)

Basis Calculation:

- Purchase Price
- Plus permanent upgrades/renovations
- Minus depreciation

Example: You buy a property for \$200,000 in 2019

Add \$25,000 in renovations

Depreciate \$30,000 over the years

Sell it for \$385,000 in 2026

What is the capital gain?

\$200,000

+25,000 Renovations

- 30,000 Depreciation

\$195,000 Basis

\$385,000 Sale Price

-195,000 Basis

= \$190,000 Capital Gain

Tax calculation has several moving parts! Don't assume a flat 15 or 20% rate!

Section 121 Exemption



- Capital gains tax exemption on profits of a personal residence
 - Up to \$250,000 for single filers
 - Up to \$500,000 for married filing jointly
- For personal residences only
 - Owner occupies the home for 24 of the last 60 months
 - Proration possible

Invest in Real Estate – 1031 Exchange

- 1031 Exchange or Like-kind Exchange
 - Defers all or some capital gains taxes for business/rental properties
 - Lots of rules here – take a 1031 exchange class for more details
 - If you defer taxes until death, your heirs will legally avoid your capital gains taxes



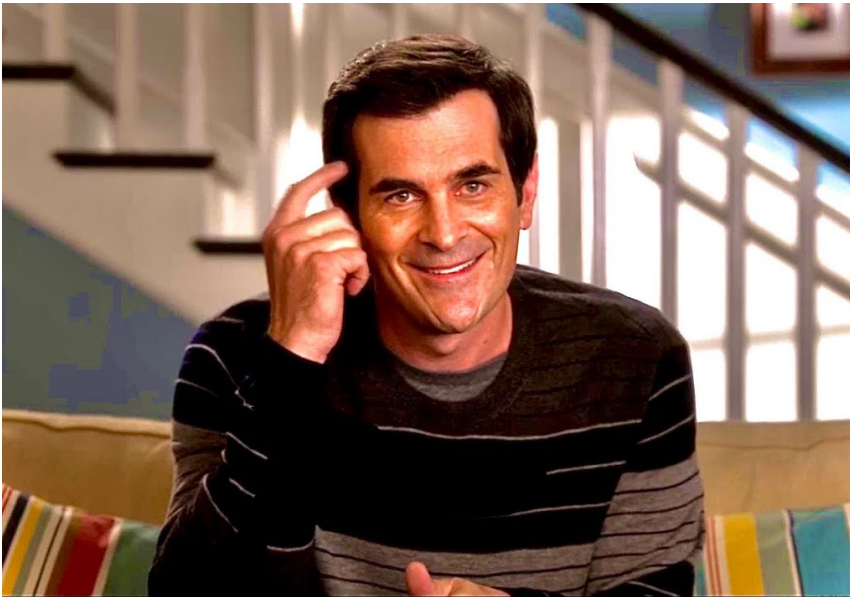
Invest in Real Estate – 1031 Exchange

1031 Exchange Example

- Phil Dunphy bought an investment property in 2015 for \$300,000. It is worth \$450,000 today.
- If he sells it he will have a capital gain of \$150,000 (depreciation and selling costs ignored). **He could owe up to \$30,000 in taxes.**



Invest in Real Estate – 1031 Exchange



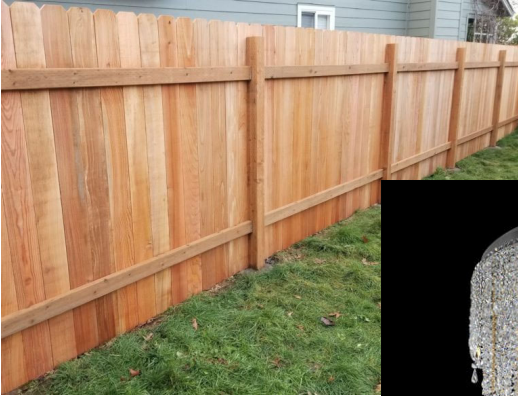
- Phil goes is under contract within 45 days for a property with a price of \$600,000. He closes within 180 days.
- **He defers \$30,000 in taxes**

Invest in Real Estate - Depreciation

- **Depreciation** - Lowers your taxable income, but not your bank account
- Can depreciate building but not land
 - Straight line (27.5/39 years) or accelerated
 - ***DOES NOT AFFECT YOUR OR YOUR CLIENTS' DEBT TO INCOME RATIO! (DTI)***



Invest in Real Estate – Cost Seg



Cost segregation study (cost seg)

- Accelerates depreciation on non-building components
- When you acquire and sell matters
- May not be worth it without enough income to offset
- Active/passive activity

Invest in Real Estate – Cost Seg

The results of this modeling effort produced the following benefit:

Additional Depreciation Deductions **\$115,644**

The following information ("Meta Data") about the property was used in the calculation:

Property Meta Data:	
Occupancy Type:	Residential
Building Use:	SFR
New Construction:	No
Construction Class:	D
Lot Area:	12197
Footprint Gross:	3332
Perimeter:	258
Number Of Stories:	1
Total Gross Sq Ft:	1550
Story Height:	9
Exterior Wall Area:	2322
Roof Slope:	8:12
Basement:	Finished
Security System:	No
Condo?	No
If Yes, % Ownership (Site)	0%
If Yes, % Ownership (Structure)	0%
Escalators:	No
Elevators:	No
Natural Gas	Yes
Roofing Material:	Composition shingles
Siding Material:	Brick

The Meta Data was compared to our database of completed Cost Seg Studies to predict the following

Component Costs:

Component Costs:	
Site Improvements	14,273
Foundation	41,998
Elevators	0
Escalators	0
Framing	30,169
Exterior Wall	81,866
Roof	24,475
Interior Structure	31,756
Finishes	71,335
Furnishes	36,505
Plumbing	29,678
Gas Distribution	1,512
HVAC	25,231
Electrical	43,270
Equipment	23,933
Total	456,000

Real Estate Professional Status (REPS)



Benefit of REPS:

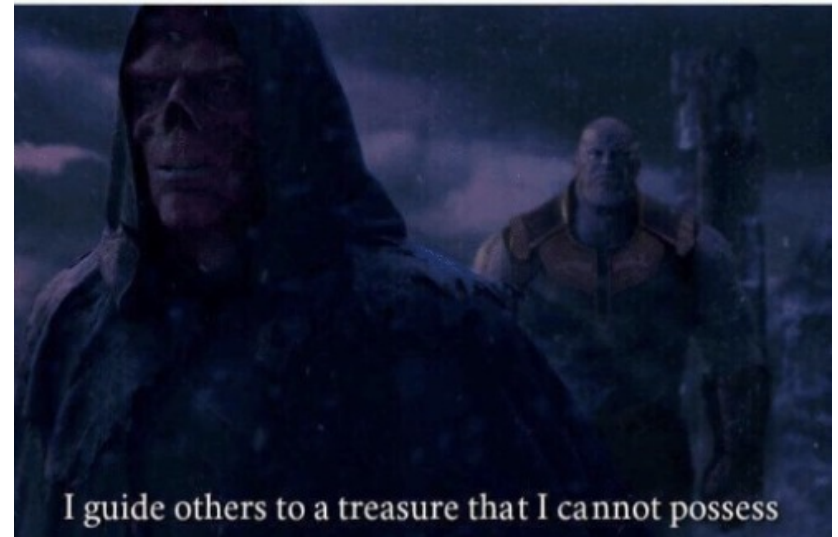
- You can take losses from rental properties (real or paper) against your commissions!
- Example: If you make \$200k in commissions and have \$150k in losses on your rental properties, your taxable income is just \$50k!
- Non-REPS generally can't do this.

Real Estate Professional Status (REPS)

A real estate professional is classified as someone who BOTH:

- Spent more than half of your work was in real estate (buying/selling/property management) AND
- Spent more than 750 hours working in RE AND more than any other job
 - Title, mortgage professionals, inspection, appraisal, etc. do NOT qualify on their respective professions alone
- Material participation in your properties
- Agent who has managed properties by someone else (PM company)
 - Rental income is passive

WHEN CPAS COACH INVESTORS
ABOUT THE TAX BENEFITS OF
REAL ESTATE PROFESSIONAL STATUS



Invest in Real Estate – STR Loophole



Short-term Rental Loophole

- Allows a non-Real Estate Professional to use a Cost Segregation Study on a STR property
- Decreases W-2 income taxes!

Invest in Real Estate – STR Loophole

- Rules

- Average stay must be less than 7 days
- Owner must actively participate in property management for at least 100 hours
- Nobody else may work on the property more than you (maintenance, repairs, cleaning, management)
- Combine with Cost Seg



Invest in Real Estate – Augusta Rule



- Augusta Rule (Section 280(a)(g))
- Rent out personal residence for up to 14 days without tax consequences
- Rent must be reasonable
- Document it!
 - Contract, receipts, bank statements, comparable quotes, board meeting minutes

Qualifying for a mortgage while self-employed



- Employees are underwritten using W-2s and paystubs
- Self-employed borrowers are underwritten using full business and personal tax returns
- Mortgage qualifying income \neq taxable income
- LOTS of self-employed people have a hard time qualifying for a mortgage because their tax preparer made them look poor

Taxes and Reverse Mortgages

- Work great for ALL income levels
- Best in concert with entire financial plan
- Pull money out of qualified IRAs tax free
- I will probably save my parents \$100k-150k in taxes



Taxes and Reverse Mortgages



\$100,000

Traditional
IRA

24% Marginal
Tax Rate

1099-R
\$24,000

\$76,000

Bank
Account

Taxes and Reverse Mortgages



\$100,000

Traditional
IRA

1099-R
\$24,000

Bank
Account

HECM
(Reverse
Mortgage)

\$100,000
Accrued Interest

1098

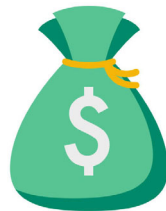
Taxes and Reverse Mortgages

Traditional
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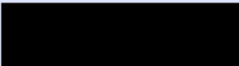

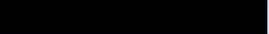







\$100,000

Bank
Account

Taxes and Reverse Mortgages

CORRECTED (if checked)

RECIPIENT'S/LENDER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no. 		*Caution: The amount shown may not be fully deductible by you. Limits based on the loan amount and the cost and value of the secured property may apply. Also, you may only deduct interest to the extent it was incurred by you, actually paid by you, and not reimbursed by another person.		OMB No. 1545-1380 Form 1098 (Rev. January 2022) For calendar year 20 <u>23</u>		Mortgage Interest Statement
RECIPIENT'S/LENDER'S TIN 		PAYER'S/BORROWER'S TIN 		1 Mortgage interest received from payer(s)/borrower(s)* \$ 195,000		
PAYER'S/BORROWER'S name 		2 Outstanding mortgage principal \$ 458,932.57		3 Mortgage origination date 1/6/2018		
Street address (including apt. no.) 		4 Refund of overpaid interest \$		5 Mortgage insurance premiums \$ 4,197.11		
City or town, state or province, country, and ZIP or foreign postal code 		6 Points paid on purchase of principal residence \$		7 <input checked="" type="checkbox"/> If address of property securing mortgage is the same as PAYER'S/BORROWER'S address, the box is checked, or the address or description is entered in box 8.		
9 Number of properties securing the mortgage 		10 Other 		8 Address or description of property securing mortgage 		
Account number (see instructions) 				11 Mortgage acquisition date 1/6/2018		

How to Give Tax Advice as a Realtor



- In short: DON'T!
- “As far as I know... but you should really ask a tax professional”
- Avoid legal liability – time, \$, license could be on the line

Questions?



Thank You!

Scan for my contact info:



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