

1031 EXCHANGE INSIGHTS

Volume 2, Issue 3

March 31, 2005



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IRS PROBES PHONY REAL ESTATE SCHEMES

Mortgage fraud and other phony real estate related schemes are on the rise, according to the IRS. The agency is combating real estate fraud through federal tax investigations and money laundering charges. IRS Criminal Investigation has doubled the number of

real estate fraud investigations from 2001 to 2003. Several common schemes that draw the attention of criminal investigators, include property flipping involving false statements to the lender; the preparation of two sets of settlement statements, including one

fraudulent statement that is given to the lender showing an inflated purported selling price; and fraudulent qualifications, where real estate agents fabricate the employment history or credit record of buyers.

Providing tax advice on like kind exchanges.

Strategic Property Exchanges, LLC serves as Qualified Intermediary on Section 1031 Exchanges, including forward, reverse, and parking arrangements.

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SELF DIRECTED PLANS UPDATE:

I spent some time last month discussing the investment of real estate by Self Directed IRAs and Roth IRAs. It also appears that owner/ participants of 401(k)s are also being advised to invest in real estate. In a conversation this week, a real estate rehabber, was advised by two large Self directed Plan promoters that he could purchase real estate, fix it up and resell it while owned by his 401(k).

I believe this to be incorrect on several points. First, buying and reselling real estate is treated as a trade or business, and is treated by the IRS as Unrelated Business Taxable Income (UBTI). UBTI is subject to income taxes

even though the property is owned by the 401(k). This defeats the whole purpose of owning real estate in a qualified retirement plan. Secondly, since this is an obvious disregard of the rules and regulations, the owner would probably be subject to tax penalties. Third, this may result in the plan being disqualified and all the amounts held in the plan being treated as a taxable distribution. Fourth, a 401(k) owning depreciable real estate loses the benefit of non cash depreciation deductions over the life of the property. Fifth, the 401(k) cannot distribute earnings from the plan until the plan participant is eligible to receive retirement distributions under the

plan, generally beginning at age 59 ½. Sixth, while property owners generally are taxed on appreciation from the sale of their real estate at 15%, income received by a plan participant is taxed at ordinary rates, @ 35%. This is a very complex area of tax law and most real estate investors have not been properly educated as to the pros and cons of owning real estate in a retirement plan. Allow Strategic Property Exchanges, LLC to guide you through various tax strategies to defer or reduce your income and gains associated in owning real estate and business property.

Coming Next Month

- What are your chances of being audited?
- Can I depreciate that?