

What Are The Common Tax Advantages Of Real Estate Investing

As an investor, you probably want to increase your profits and minimize expenses. And if you have chosen the real estate industry as your investment, then you're in luck because the tax advantages are abundant.

From depreciation expenses to exemption from the FICA taxes, the incentives can significantly reduce your taxable income, thereby increasing your net earnings.

Of course, you must ask the [real estate license](#) professionals to guide you through the filing. All of these factors are combined to make real estate as one of the most tax-efficient investment options available today. In this article, you will learn the benefits of real estate investing and understand why it's a good investment.



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Use of Real Estate Tax Write-Offs

You'll be thrilled that real estate investing allows you to take advantage of incredible tax write-offs. This will significantly reduce your financial burden.

The IRS grants property investors the opportunity to deduct various expenses associated with acquiring, operating, and managing their properties.

Costs such as interest in mortgage, property taxes, operating expenses, depreciation, and even repairs or improvements made on the property can be written off. Making these deductions can lower the taxable income, reducing the money you owe in

taxes.

Depreciation is one of the most significant deductions real estate investors are willing to capitalize on. Also, it's a non-cash expense allowing you to deduct a portion of the property's cost each year over the useful life defined by IRS guidelines.

Another notable expense is the mortgage interest. As long as the loan is used in buying or improving the rental property, all the incurred interest can be written off against rental income.

Depreciation Costs

Over time, the value of a property may depreciate because of the need for fixing and wear and tear. But don't fret – the depreciation can be deducted from the annual income, potentially saving you a significant amount on your taxes.

And it's something most real estate license professionals would advise. Therefore, depreciation is a non-cash expense that reduces taxable income without immediate cash outlays.

But remember, when you sell your investment property down the line, there will be potential implications called the 'depreciation recapture,' where some or all of the written-off value gets taxed upon sale unless specific strategies are used.

So always consult with a tax advisor or CPA, and even professionals with real estate license who specializes in real estate investing, before making any decisions based on these benefits.

FICA Tax/Self-Employment

When you are a self-employed individual, you would be the one

responsible for the employee and employer portions of the Federal Insurance Contributions Act (FICA) tax. However, for someone who invests in real estate and actively participates in rental activity, you may avoid paying some or all of this hefty tax.

Here's how it works: The IRS views the rental activities as passive by default unless you are considered a 'real estate license professional.' This means that most part-time landlords will not have to pay employment taxes on the rental profits because they are not considered active participants in business operations.

However, you must be careful with the classification because it's not just about the time spent but also the regularity and intensity of the work.

You must consult a knowledgeable tax advisor before making any definitive decisions regarding your tax status!

Passive Income and Pass Through Deductions

Understanding the passive income and even the pass-through deductions can be a game-changer. Passive income is the earning from rental properties, limited partnerships, or other enterprises in which you're not actively involved.

It's important to consult a tax professional or accountants familiar with real estate investing to ensure you're maximizing the potential savings while staying within IRS guidelines.

Short and Long-Term Capital Gains

The short-term capital gains apply when the property was owned for less than a year and is being taxed at the ordinary income

tax rate. On the other hand, the long-term capital gains offer significant tax advantages compared to their shorter counterpart. Most taxpayers fall into the 15% bracket for long-term capital gains taxation – considerably lower than typical income tax rates!

Moreover, those in the 10-15% ordinary income tax bracket may qualify for a zero percent long-term capital gain rate! Yes, zero percent! And even at its highest tier (20%), it's still notably less than top marginal income tax rates.

So you better hold onto real estate investments longer because it will allow potential appreciation and provide substantial savings from lower taxes on any profits made from sales.

Opportunity Zone Funds

Opportunity Zone funds are designed to incentivize development in economically distressed neighborhoods. Investing in these areas can reap significant tax benefits while contributing to community improvement.

Keep it for seven years, and the reduction will increase to 15%. And if you can manage to maintain the investment for ten years? Well then, any additional gains accrued from the opportunity zone investment will be tax-free when they're sold or exchanged.

So not only do Opportunity Zone Funds help stimulate economic growth in underprivileged communities, but they also provide an exceptional way of maximizing potential tax benefits from real estate investments.

Defer Taxes with Incentive Programs

Leveraging incentive programs can prove to be a wise strategy for deferring the burden of taxes, thereby bolstering your overall return on investment.

Several such programs exist at both the federal and state levels to encourage property development or rehabilitation in certain areas, which can result in significant tax savings for savvy investors.

Bear in mind that there are specific rules and timelines to follow here; failing to do so could lead to forfeiture of this benefit.

Conclusion

Now you know the tax advantages of real estate investing. With strategies like depreciation write-offs, FICA tax reductions, and capital gains considerations, your investments can work harder for you.

Remember, the tax landscape in real estate can be complex. Always consult with a professional, even professionals with real estate license, for they are well-versed in tax laws and regulations to ensure precise financial analysis.