

## Tax Shelters

Example: Truck tractor unit, original cost \$60,000

	<i>Depreciation deduction</i>	<i>Rental income</i>	<i>Operating profit (loss)</i>
2016	\$20,000	\$ 5,000	(\$15,000)
2017	\$26,667	\$19,000	(\$ 7,667)
2018	\$ 8,889	\$19,000	\$10,111
2019	\$ 4,444	\$19,000	\$14,556
2020	-0-	\$19,000	\$19,000
2021	-0-	\$14,000	\$14,000
<i>Total</i>	<i>\$60,000</i>	<i>\$95,000</i>	<i>\$35,000</i>

### “Passive activity”

- Trade or business in which taxpayer does not materially participate
  - Example: limited partner
- Any rental activity
  - Exception: “Mom and Pop” rental house
  - Exception: Real estate professionals

### Income Splitting (Attribution of Income)

- No splitting of personal service income
- Income from property
  - No “carving out”  
Reversion - IRC § 673
  - No retained economic interests  
Right to revoke - IRC § 676
  - No retained power to change beneficial enjoyment  
Right to change beneficiaries - IRC § 674

Accumulation trusts - IRC § 1(e)

“Kiddie” tax - IRC § 1(g)

## Capital Gain and Loss

Why do you care?

- IRC § 1(h)
  - Preferential rates for “net capital gain”
  - IRC § 1222(11) - long-term capital gain
- IRC § 1211(b)
  - Capital losses deductible only against capital gain (\$3,000/year ordinary income)

What is capital gain or loss?

Gain [loss] from the *sale or exchange* of a capital asset (IRC § 1001)

Dividends on stock also taxed at capital gain rates - IRC § 1(h)(11)

What is a capital asset?

Everything! Except what’s listed in IRC § 1221(a):

- (1) Inventory and property held for sale to customers
- (2) Depreciable property, and real estate used in a business\*
- (3) Self-created © (other than music), manuscript, etc.
- (4) Business accounts receivable
- (5)-(7) Esoterica
- (8) Supplies

\* Depreciable property, and real estate used in a business -  
IRC § 1231

- Losses are ordinary
- Long-term gains are capital (best of both worlds!)
  - Except gain that is “depreciation recapture”  
IRC §§ 1245, 1250

## Depreciation recapture

### Equipment - IRC § 1245

- Gains are ordinary to extent of depreciation previously taken
- Any amount realized in excess of original basis (unusual) = Sec. 1231 gain (capital)
- Losses are ordinary per IRC § 1231

### Depreciable real property - IRC §§ 1(h)(7), 1250

- Gains are capital (Sec. 1231), but top rate is 25% - IRC § 1(h)(6)
- Losses are ordinary