BIOGRAPHY

Michael Lantrip, Attorney at Law, is licensed to practice law in Texas, North Carolina, Virginia, and the District of Columbia.

He has a B.B.A. in Finance from the University of Houston School of Business, and he has a Juris Doctor (J.D.) in Law from the University of Texas School of Law.

He is admitted to practice in all Courts in Texas, North Carolina, Virginia, and the District of Columbia, as well as the U.S. Tax Court, U.S. Federal District Court, Eastern District of Texas, and the D.C. Court of Appeals.

He practices in the fields of Tax Law, Real Estate Law, Corporate and Business Law, and Wills, Trusts and Estates.

Formerly a Tax Examiner for the IRS, and a Tax Accountant for a Big 8 Accounting Firm, he has also been a Newspaper Reporter, Radio Announcer, Radio News Director, Television Reporter and Anchorman, Television Executive News Producer, and Military Intelligence Analyst.

In addition to 35 years of practicing law, he built one of the first computerized Abstract Plants and operated his own Title Insurance Company, and has been an Approved Title Attorney for seven national Title Insurance Underwriters.

He has handled over 2,000 real estate closings.

Prior to his law career, he was a Radio Announcer at WQTE in Detroit during the "Motown" era, and he was a DJ at KIKK in Houston when it was named "Country Music Station of the Year" by Billboard Magazine.

He has written and produced more than 1,000 half-hour Television Newscasts.

He has written over 700 stories as a daily Newspaper Reporter.

He has logged over 8,000 hours on the radio.

He is a Lifetime Member of Mensa.

He has written and published four books:

"How To Do A Section 1031 Like Kind Exchange"

"50 Real Estate Investing Calculations"

“Tax Cuts And Jobs Act For Real Estate Investors”

“Your Best Business Entity For Real Estate Investing”

All are available in print and digital on Amazon.

His Amazon Author Page is:

amazon.com/Michael-Lantrip/e/B01N2ZRGUY

His personal website is MichaelLantrip.com.

SECTION 1031 STATUTE

"No gain or loss shall be recognized on the exchange of real property held for productive use in a trade or business or for investment if such real property is exchanged solely for real property of like kind which is to be held either for productive use in a trade or business or for investment."

SOME CLARIFYING DEFINITIONS

"Exchange" does not (only) mean trading one for another, as with baseball cards. Exchange means divest yourself of one investment and replace it with another.

This can be done in four ways:

1.) SIMULTANEOUS. Straight-up trade, one property for another, with or without Boot on either side.
2.) DELAYED. Sell one property and, within 180 days, buy another one.
3.) REVERSE. Buy your new property and within 180 days, sell your existing property.
4.) CONSTRUCTION. Build or rehab a new property and then sell your existing one.

"Real property" means the type of investment property involved. Section 1031 no longer covers personal property investments such as art works and airplanes. But it does include, in my opinion, the "personal property" that is part of the real property investment, such as refrigerators, furniture, and washers and dryers.

"Like kind" means that the new property is real estate, and

"is to be held" means that the new property will also be held for productive use in a trade or business or for investment.

SECTION 1031 RULES

The "rules" of Section 1031 are not written down somewhere that you can go and read them.

Rather, they have evolved, from the statute, from IRS Revenue Rulings, and, to a lesser extent, from Private Letter Rulings.

And, as the various positions of the IRS were tested in the U.S. Tax Court and the Federal District Court by the taxpayers, a generally-accepted body of rules have come into existence.

Here are 10 of them.

<u>One.</u> Both properties must be business or investment properties.

For your Relinquished Property this means that you must have owned it and used it for a sufficient period of time to establish its identity and character as a business or investment property. Usually, the time period is more than 1 years.

For your Replacement Property, it has no identity or character when you acquire it, except that it is "to be held for productive use in a trade or business or for investment."

To fully qualify for the Section 1031 Exchange, you must then actually hold it for productive use in a trade or business or for investment.

The holding period is at least a year and a day, and at least two tax years.

<u>Two.</u> Replacement Property price must be equal to, or greater than, the sales price of the Relinquished Property.

<u>Three.</u> All of your Net Sales Proceeds from the sale of your Relinquished Property must be used in the purchase of your Replacement Property.

Four. The name that goes on the deed when you receive title to the Replacement Property must be the same name that was on the deed that transferred title of the Relinquished Property.

Five. The date that you sell the Relinquished Property is called the Exchange Date, and you have 45 days to identify in writing to your QI a list of the possible properties that you will purchase as your Replacement Property.

You have three choices of how to do this.

First, you can identify up to 3 properties without regard to the value of each and without regard to the total value of all three together.

Second, you can identify as many properties as you want, as long as the total value of all of the properties is not more than 200% of the value of the Relinquished Property.

Third, you can identify as many properties as you want without regard to value, as long as you end up closing on enough of the properties to represent 95% of the total value of all of them.

Six. Within 180 days after the Exchange Date, you must close on the purchase of your Replacement Property.

Seven. You cannot sell your Relinquished Property to, or purchase your Replacement Property from, or swap properties with, a person related to you, a "related party," without having certain restrictions imposed.

A related party is your spouse, brother, sister, child, grandchild, parent or grandparent.

A related party also includes a corporation, partnership, LLC, or similar business in which you own more than 50% of the interest.

<u>Eight.</u> You cannot have actual receipt of, constructive receipt of, or control over, the Net Sales Proceeds from the sale of the Relinquished Property.

The Net Sales Proceeds must be held by the QI.

The QI is a totally unregulated entity. There are only 6 states that have bothered to place any requirements, such as bonding or insurance, but no licensing or monitoring in any way: NH, VA, WASH, NEV, COLO, CAL, and MAINE.

PA doesn't have to because they don't recognize Section 1031 in their State tax laws.

<u>Nine.</u> You claimed Depreciation on your property each year that you owned it and operated it as investment property, 27.5 years for residential real estate and 39 years for commercial real estate.

When you sell, there will probably be Basis still in the property that has not been claimed as Depreciation. You have two choices for what to do.

First, you can actually continue to claim Depreciation on this property even though you no longer own it. Identify it on your Depreciation Schedule as "Section 1031 Relinquished Property Basis."

Your second choice is to add the Undepreciated Basis, called your "Transferred Basis," in the Relinquished Property to the newly-created Depreciable Basis in the Replacement Property and add the new asset to your Depreciation Schedule.

Either way, you must tell the IRS what you decided to do. This is called "making an Election."

When you file your next Form 4562, Depreciation and Amortization, check the box that says, "Election Made Under Section 1.168(i)-6T(i)."

Ten. There is a mistaken belief that one of the Rules of Section 1031 is that the new Mortgage on the Replacement Property must be at least as much as the Mortgage that was paid off at the closing on the Relinquished Property.

This is not correct.

You can add your own cash for all or part of the additional funds needed.

But if you do not add cash, the new debt created will be at least equal to the debt paid off just because that's the only thing that will work.

FREE MONEY TIMES 4, THEN TIMES 19

This is a simplified view of a real transaction intended to demonstrate the power of Section 1031, and the concept of "free money."

We are assuming:

One. You sold and investment property and your Capital Gains is $250,000. We are ignoring transaction costs for the sake of simplicity and assuming that there was no debt on the property to be paid off.

Two. Your other Taxable Income is $250,000 and you are MFJ. So, your CG Tax Bracket is 15%. We will assume another 5% in State Tax, for a total of 20%. (PA does not recognize Section 1031 for State tax purposes.)

Note: following CG Tax Brackets.

SINGLE	0 - 39,375	0%
	39,376 - 434,550	15%
	Over 434,550	20%
MFJ	0 - 78,750	0%
	78,751 – 488,850	15%
	Over 488,850	20%

Three. Your Capital Gains liability will be 20% of $250,000 = $50,000.

It would actually be more, because some of the $250,000 CG would represent Depreciation Recapture, which is taxed at 25% for Straight-line Depreciation and up to 37% for Accelerated Depreciation, but for simplicity and to illustrate the concept, we will use 20%.

Four. If you don't do a Section 1031 Exchange, you will send the $50,000 to the IRS and the State, and the money will be gone forever. You will be left with just the $200,000, to do with as you please.

Five. However, you can do a Section 1031 Exchange and use the entire $250,000 to buy another investment property.

Six. We will break it into two purchases, so that we can track the results of being able to keep the $50,000 of tax liability and using it for investment, instead of giving it to the government.

Seven. You use $200,000 as a Down Payment, get a 75% loan for $600,000, and buy an investment property for $800,000. We won't track that investment.

Eight. You use the $50,000 as a Down Payment, get a 75% loan for $150,000, and buy an investment property for $200,000.

Nine. This is why I call it "Free Money Times Four." Your $50,000 of free money ends up being $200,000 available to you for investment.

Ten. Now, let's look at what happens in just 10 years. We will assume a 6% annual appreciation in value for the property, even though the historic annual average is 6.7%.

Eleven. In 10 years, the FMV of the property will increase from $200,000 to $358,170.

Year 1	200,000 x 1.06 = 212,000	12,000
Year 2	212,000 x 1.06 = 224,720	12,720
Year 3	224,720 x 1.06 = 238,203	13,483
Year 4	238,203 x 1.06 = 252,495	14,292
Year 5	252,495 x 1.06 = 267,645	15,150
Year 6	267,645 x 1.06 = 283,704	16,059
Year 7	283,704 x 1.06 = 300,726	17,022
Year 8	300,726 x 1.06 = 318,770	18,044
Year 9	318,770 x 1.06 = 337,896	19,126
Year 10	337,896 x 1.06 = 358,170	20,274

1.06 to the 10^{th} power = 1.790847

1.790847 x 200,000 = 358,170

Rule of 72: 72 divided by 6 = 12

Twelve. The FMV of the $200,000 property has risen to $358,170 and that is a factor of 179%, or an ROI 79%.

Thirteen. Your Equity in the property, assuming a Note Paydown to $120,000, is now $238,170.

Fourteen. This is an Equity increase of 475%.

Fifteen. And the $50,000 wasn't even your money. It was the IRS's.

Let's look at what happens if you cash out at this point. We are ignoring transaction costs.

And we assigned $20,000 to the value of the land and depreciated the $180,000 building for 27.5 years, which is $6,540 per year.

DEPRECIATION = 65,400

PROPERTY BASIS = 134,600

CAPITAL GAINS = 158,170 & 223,570

GROSS SALES PROCEEDS	358,170
LESS: NOTE PAYOFF	(120,000)
NET SALES PROCEEDS	238,170
CG TAX (.20 X 158,170)	(31,634)
DEPRECIATION RECAPTURE (.25 X 65,400)	(16,350)
PAYMENT OF DEFERRED TAX*	(10,000)
CASH TO SELLER	180,186

DEFERRED TAX: The original Capital Gains that was deferred was $50,000 and one-fifth of the Capital Gains was used for this investment, so one-fifth of the deferred amount must now be paid.

So, you have turned the $50,000 of the IRS's money into $180,186.

This is a 260% ROI in 10 years. Except that it is really an infinite return because it was not your money.

BUT, if you sell and do a Section 1031 Exchange, the numbers are entirely different.

You defer the taxes on the Capital Gains and the Depreciation Recapture, and roll them into another property.

You use the entire $238,170 for a 25% Down Payment, and get a 75% loan for $714,510 to purchase a new investment property for $952,680.

You could be looking at a smaller Apartment Building, or a couple of Fourplexes, or maybe four Duplexes. You could even consider a small strip shopping mall.

The $50,000 that you held back from the IRS has now become over $950,000 worth of income property, an increase of 19 times, in just ten years.

And, again, it wasn't even your money.

We can also look at the other $200,000 of the $250,000 in Capital Gains that was invested in the other property.

Assuming the same 1.79085 increase in value, the $800,000 property that you bought with the $200,000 Down Payment, the FMV is now $1,432,600 with a paid-down Note Balance of $600,000.

Sale of this property would result in $832,600 in Net Sales Proceeds for you to use as a Down Payment, which would allow you to purchase a new Section 1031 Exchange property for $3,330,400.

Ten years after a $250,000 Capital Gains sale, you are holding title to $4,283,080 worth of investment rental property.

In addition to the cash flow and tax benefits, it is appreciating in value more than $250,000 each year.