Part 3 of “40% in Taxes… Are You Kidding Me??”

This article is the final installment of a three-part article. In the first article, I discussed the possibility of having to pay nearly 40% in taxes for the sale of appreciated real property and discussed two techniques that are available to defer the payment of capital gains taxes (the 1031 exchange and an installment sale.)

Last month, I outlined two additional options that could be used to defer or eliminate capital gains taxes. The deferred sales trust can be used to defer the payment of capital gains taxes for 20-30 years that are owed on the sale of appreciated real estate, while the capital gains elimination trust eliminates the payment of capital gains taxes entirely. Please note that I am neither an attorney nor a certified public accountant and recommend that you seek outside professional counsel before engaging in the following potential strategy.

Split Interest LLC—In this approach, a limited liability company (“LLC”) is coupled with a non-profit organization as a limited partner. This type of business structure eliminates capital gains taxes upon the sale of an appreciated asset that has been transferred into the LLC. Your annual income will vary somewhere between 3-10% of the asset, and depends on your degree of involvement as well as the type of asset transferred into the LLC.

*Advantages:*

- Provides you with tax-free income for the duration of your life.
- Creates substantial income tax deductions for at least 6 years and possibly even more.
- Creates no tax on investment earnings, which means that there are no income taxes on the investment earnings, no capital gains taxes on asset sales, and no estate, gift, or generation skipping taxes on the assets put into the plan.
- Creates asset protection by removing the assets from the reach of your creditors.
- Provides you with complete and unrestricted control over your assets.
- Passes control over the assets to your heirs at the time of your death, if you desire to do so.
- Creates the opportunity to provide income payments to any number of charities and to make a large endowment at the time of your death, if you desire to do so.
- Creates the opportunity to make future contributions to the plan, if you desire to do so.

*Disadvantages:*

- Higher cost to initially structure than the other techniques we have already discussed and there are more “moving parts.”
- While the tools used in this strategy are commonplace, the combination of tools is relatively new and the IRS has not provided any formal guidance.

Over the last two to three years, by far the greatest interest has been in the Split Interest LLC, which retains control for the individual/family selling the real estate or other appreciated asset. Retaining control *plus* eliminating 99% of the taxes upon the sale *plus* asset protection make this a viable tool in the sale of an appreciable asset of $1 million or greater.

R. J. Kelly is the Founder and Chief Visionary Officer of the Wealth Legacy Group, Inc. in San Diego, CA.  Learn more about R. J. and Wealth Legacy Group at www.wealthlegacygroup.com, or call (800) 975-5355.