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Tax code rewrite favors real estate over art

Since the recent tax code overhaul, some of your clients may be confused about whether acquiring art or real estate would be a better investment for their estate and financial planning purposes.

Congress kept the 1031 exchanges that allow real estate to be sold tax-free if the proceeds go to buy more property. That same advantage for art collectors - and classic car aficionados such Jay Leno - disappeared in the new tax code, which means anyone who sells art could be hit with a nearly 30 percent tax on the gains, according to a recent report by *The New York Times*.

Land ho!

The 1031 exchange is important because it can allow property owners to conceivably pay no tax on their property - ever, the *Times* says. That's because the estate tax exemption was raised to $11.2 million for individuals and $22.4 million for couples.

Your clients could use the exchanges to buy increasingly more valuable property until they die, at which point the capital gains tax is eliminated. Their heirs then inherit the real estate at what it's worth at that time, so that initial $1 million investment that's rolled over into new properties several times could be worth many millions more, tax free.

Imagine if one client bought property in Silicon Valley 20 years ago, when the tech boom was still in its embryonic stages, and another client invested the same amount of money in Apple stock. Both would have seen huge gains in the ensuing years, making a ton of money for those clients. That's where the similarities end.

The real estate owner today could sell that property and buy another one in Silicon Valley - or anywhere else in America - without paying tax on the original property's appreciated gains. But if the Apple stock owner sold and bought into other technology companies, he would be subject to a capital gains tax of 20 percent.

Art fare

Originally designed to help support home building, and more broadly the housing market in general, Section 1031 allowed for a "like-kind" exchange, which savvy investors used in the art market as well, reported *Artsy.net*. But the new law eliminates use of this provision for tangible, or portable, assets such as art and classic cars.

The effect, says the *Times*, is that museum quality art might wind up outside the United States. Collectors, or your clients, who might have spent significant money on a single work of art can no longer take advantage of the 1031 loophole to turn that into other works of art without paying tax on the gains.

Major collectors such as financial trader Steven A. Cohen or casino magnate Steve Wynn usually place their artwork in museums, says the *Times*, but that could wane with the new law.

Reaching for a piece of art doesn't make as much sense in this climate, whether for a major investor or your client who is a patron of a local art gallery. Real estate appears to be the wiser choice.

We hope this information is useful to you and helps your client and their families. If you have a specific case or question, please don't hesitate to call our office.