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Re: What the New Tax Bill Means for You

Dear Titan Pacific Client,

Earlier this week, lawmaker's in the House and Senate passed sweeping tax reform legislation that the President signed into law today. Throughout the past few weeks leading up to the passage of this new tax bill, I have had conversations with several clients who wanted to discuss the potential impact that this new tax bill could have on the real estate market and more specifically, what it might mean for themselves and their families. With this new measure going into effect on January 1st, 2018, as part of our ongoing effort to help keep clients informed about the current and future state of our local Southern California real estate market, it seems appropriate to provide the following summary of the recently passed tax bill, which will hopefully be a helpful high-level overview of what this new legislation means for homeownership and real estate investing.

First and foremost, it is important to keep in mind that determining whether the new tax law will save you money or cost you money depends on a number of factors that relate to just about every aspect of your financial life. Your employment status (i.e. salaried employee versus independent contractor); the particular line of work you are in (i.e. service category for professional service providers); and whether you are a business owner or partner in a business along with the type of entity that business is, will all likely influence the tax treatment that you receive. For example, a pass-through entity like an LLC with depreciable property assets such as real estate could receive very favorable tax treatment under the new law. Therefore, I highly recommended consulting your tax professional to better understand the complete picture of what this new tax bill means for you, and then, we can discuss the right moves for you to make on the real estate front.

With all of this being said, in the interests of keeping this summary brief and generally applicable, I will limit the items discussed in this letter to just the handful of elements that most everyone seems to be wondering about, those relating to how the new tax law will affect homeownership and mortgages.

The new tax law contains several changes that alter whether and how homeowners deduct mortgage interest and property taxes. Please keep in mind that many of these new revisions for individuals and families are set to expire at the end of 2025.

These five items could most directly affect homeownership and home buying/selling:

1.) **Mortgage Interest Deduction.** The mortgage interest tax deduction is commonly explained as a way to make homeownership more affordable. This is because it cuts the federal income tax that qualifying homeowners pay by reducing their taxable income by the amount of mortgage interest that they pay. Aside from a couple of exceptions described below, under the new tax law, starting in 2018 (for people who buy homes on or after December 15, 2017), the deduction is reduced from interest on debt up to $1 million ($500,000 if married filing separately) on your primary home and on a second home to interest on debt up to $750,000 ($375,000 if married filing separately). The new lower limit does not apply to:
    - People who were under contract to buy a home before December 15, 2017, as long as they were scheduled to close by January 1, 2018; or
    - People who refinance an existing mortgage, the new loan is treated as if it was originated on the old loan's date.

2.) **Mortgage Interest Deduction for Second Homes.** The new tax law allows you to deduct interest on mortgage debt on your primary home and a second home. However, as described in item number 1 above, it reduces the amount of eligible mortgage debt.

3.) **Property Tax Deduction.** The old tax law allowed qualifying taxpayers to reduce their taxable income by the total amount of property taxes they paid. Starting in 2018 under the new law, the deduction is limited

to a total of $10,000 ($5,000 if married filing separately) for a combination of property taxes and either state and local income taxes or sales taxes.

4.) **Home Equity Deduction.** In addition to the mortgage interest deduction, the old tax law added a deduction for interest paid on up to $100,000 of home equity debt "for reasons other than to buy, build, or substantially improve your home." For example, under the old law, if you borrowed from a home equity line of credit to pay tuition, then the interest you paid was tax-deductible. Beginning in 2018, this deduction is eliminated.

5.) **Impact on Itemizing vs. Use of the Standard Deduction.** Fewer taxpayers in higher income tax states like California will itemize under the new law because the standard deduction for married filing jointly rises to $24,000 (up from $12,700 under the law through 2017). For example, under the law through 2017, if you're married filing jointly and you paid $15,000 in mortgage and property taxes in 2017, then you would likely itemize those deductions because they exceed the standard deduction of $12,700. If you're like the hypothetical family above, then your $15,000 in mortgage interest and property taxes is less than the new standard deduction, so you will likely use the standard deduction instead of itemizing.

These are five tax decisions to consider before the year's end:

1.) **Pay Property Taxes Early.** If your state and local taxes will be greater than $10,000, you could pay the second installment bill by December 31st.

2.) **Make Extra Mortgage Payment.** Those who itemize on their returns could make their January mortgage payment in 2017.

3.) **Give More to Charity.** If itemizing, consider making 2018 charitable contributions by December 31st.

4.) **Defer or Accelerate Income.** Families with three or more kids could accelerate their income into this year.

5.) **Use Expiring Deductions.** Deductions for some unreimbursed business expenses will disappear through 2025.

Some things will not change under the new tax law, for example, **capital gains remain unchanged.** When you sell a house, the capital gain is the difference between the price you paid for it and the price you sold it for. This capital gain is treated as taxable income. However, if you owned the house long enough, you're allowed to exclude up to $500,000 ($250,000 for married taxpayers filing separately) of this capital gain as income so you don't have to pay federal income tax on it. While the House and Senate had voted to limit the capital gains exclusion, they struck that language from the final bill, so the new law does not alter the capital gain exclusions for homes.

As discussed earlier, it is also notable that the legislation provides a **new tax break for pass-through entities** through a provision that offers a 20% deduction for pass-through entities such as Limited Liability Companies, Limited Partnerships, and S-Corporations with depreciable property (such as real estate). Pass-through entities do not pay corporate taxes and instead 'pass-through' the income to company members / partners who pay individual taxes on it. Note, there are significant advantages of this portion of the law relating to real estate ownership structure that I will be happy to discuss with you.

Before concluding, I would like to quickly put our perspective on all of this into context. At Titan Pacific, we believe that homeownership has been and will always continue to be the foundation of opportunity for Americans across our great nation, and this will continue to be especially true in higher-demand housing markets like our local Southern California region where the proven value of investing in real estate as a powerful wealth generating vehicle and driver of our local economy has been clear whether the real estate asset in question is someone's primary residence or an income property.

In today's market, having the right real estate partner is essential to making sound financial decisions. I want you to know that our overriding objective is to facilitate the most favorable financial outcome for each individual client, so we unequivocally measure our success by the quality of the results we achieve rather than the number of transactions we execute or investment deals that we put together. We will continue to further this objective through our core business philosophy of "partnering for success" which is an integrated framework and our philosophical approach to real estate sales and investments through which we engage with each individual client as if they are our own investment partner, whether the situation at hand involves the sales side of our business (i.e.

when we represent a client on the purchase or sale of a primary residence) or our investments practice (i.e. buying cash flowing properties, syndicating investment deals, or developing real estate projects).

I hope you found this summary helpful and I look forward to partnering with you for success in 2018 and beyond. Please feel free to call my cell phone at 858-232-5712, or our office line at 949-464-7639 if you have any questions about this recent tax overhaul legislation or if you want to discuss anything else real estate related. You can also reach me by email at omid@titanpac.com.

Sincerely,

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