**Tax Benefits to Qualifying as a Real Estate Professional**

If you own rental real estate as a part of your overall investment portfolio, it is important to understand the tax rules to maximize your investment returns by paying less in taxes. For many real estate investors, especially those who finance their rental properties, the rental properties will produce a loss for tax purposes (often due to the depreciation expense deductions).

The tax planning question then becomes: can I deduct this loss against my other income? Like most tax questions, the answer is “maybe.”

**Question #1:** Is your income $100,000 or less per year?

If yes- you are allowed a maximum loss on all rental properties of $25,000 per year against other income.

If no- if your income is between $100,000 and $150,000 per year, you are qualified to claim a reduced exclusion. In essence, you lose the ability to deduct $1 of rental property losses for every $2 of income above $100,000. Once your income reaches $150,000 per year, all losses are phased out for the year in question.

If you can’t take the losses because your income exceeds $150,000 per year, the losses become “passive” and can only be used against other passive income for the year. Barring any passive income to offset, the losses then are carried forward to the future until they can be utilized. Thus, the losses can be used at some point in the future and it is simply a timing issue as to when.

**Question #2:** Is there a way I can deduct the losses against my ordinary income in this year even though I make more than $150,000?

Yes- if you qualify as a real estate professional.

**Question #3:** How do I qualify as a real estate professional?

* You must spend more than one-half of your “work time” (the services you perform as an employee or in any businesses that you may operate) in real estate. Simply, do 1you spend more working on real estate activities than non-real estate activities? If yes, then you must also satisfy the next bullet point:
* You must spend more than 750 hours per year working in your real estate business and you must materially participate in the real estate activities. To satisfy the 750 hour rule, you must log your time spent on your real estate activities. This time can include time spent locating and purchasing your properties, managing your rental properties (including meeting with property managers, tenants, etc.), construction, conversion or renovation of commercial or residential real estate (including all meeting times with various professionals and contractors), and the development of vacant land.

**Question #4:** I qualify as a real estate professional. What does it mean?

You can claim all losses from your rental activities against any ordinary income that you may have. For instance, if you make $300,000 per year in W-2 wages and you have $30,000 of losses from your rental properties, you will pay income taxes on the full $300,000 if you are not a real estate professional and the $30,000 of losses are carried forward into the following year. If you are a real estate professional, all of the $30,000 of losses could be used to offset some of the $300,000 of income, resulting in only $270,000 of income being taxed for income tax purposes. This would result in tax savings of approximately $10,000 in this year.

**Final thoughts:** Work with a tax professional who understands the passive activity loss rules, Internal Revenue Code Section 469 (and its permutations) and the aggregation rules for rental real estate. This is “tax geek code” for the fact that this stuff gets very complicated!