

**Second Homes and Investment Properties
Acquisition, Ownership, Disposition**

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Introduction



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Second Homes and Investment Properties

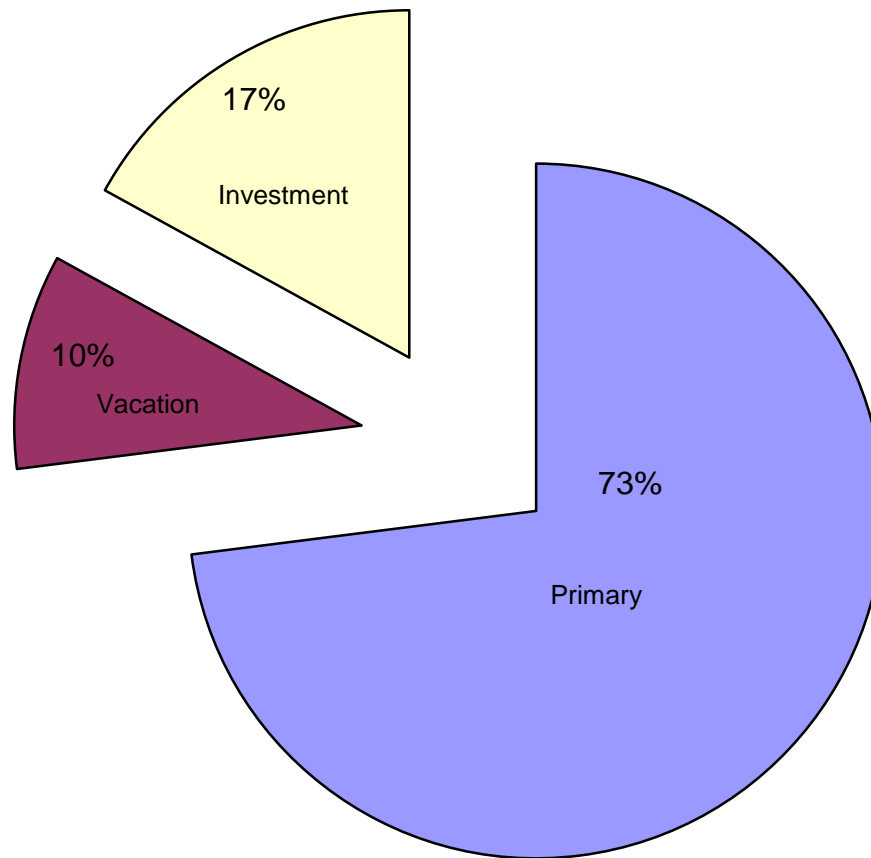
- Acquisition
- Owning and Operating
- Disposition

US Home Sales by Year

- 2007 5,040,000
- 2008 4,110,000
- 2009 4,340,000
- 2010 4,190,000

Source: National Association of Realtors

Share of 2010 US Home Sales

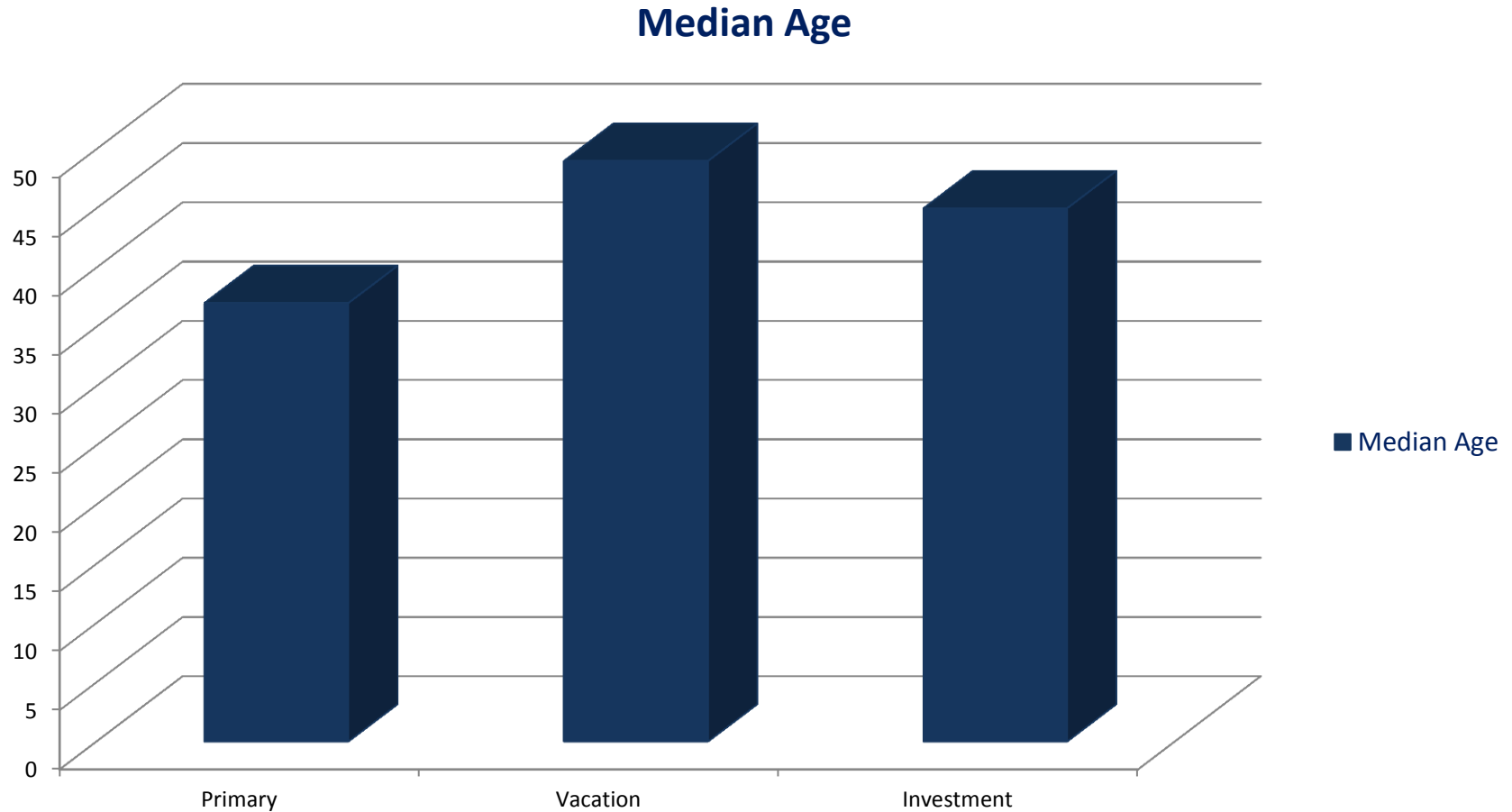


Source: 2011 NAR Survey of Investment/Vacation Home Buyers

They're your clients!

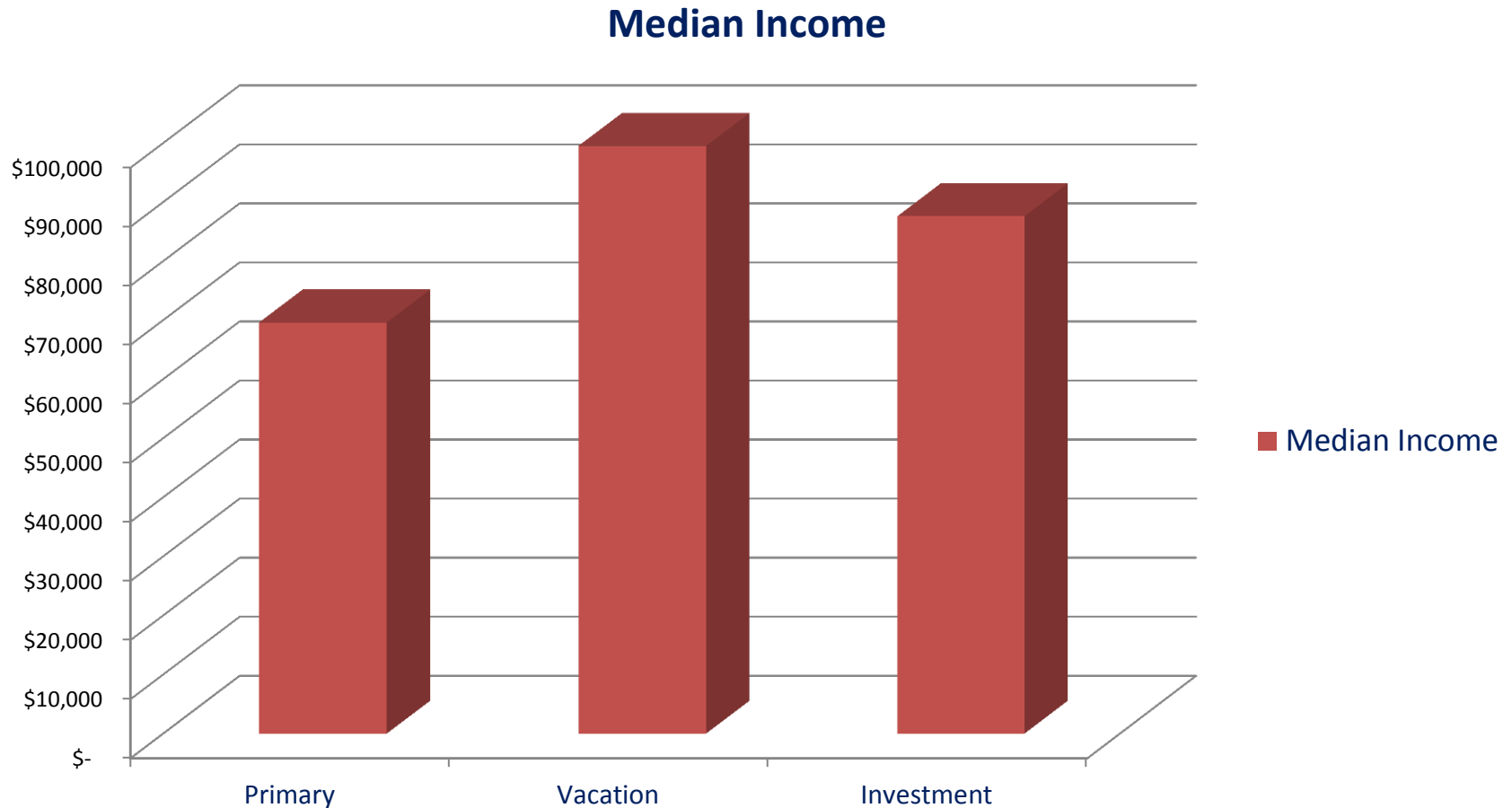
- Over one million people buy a second home or investment property every year!

Median Age of Investment/Vacation Home Buyers



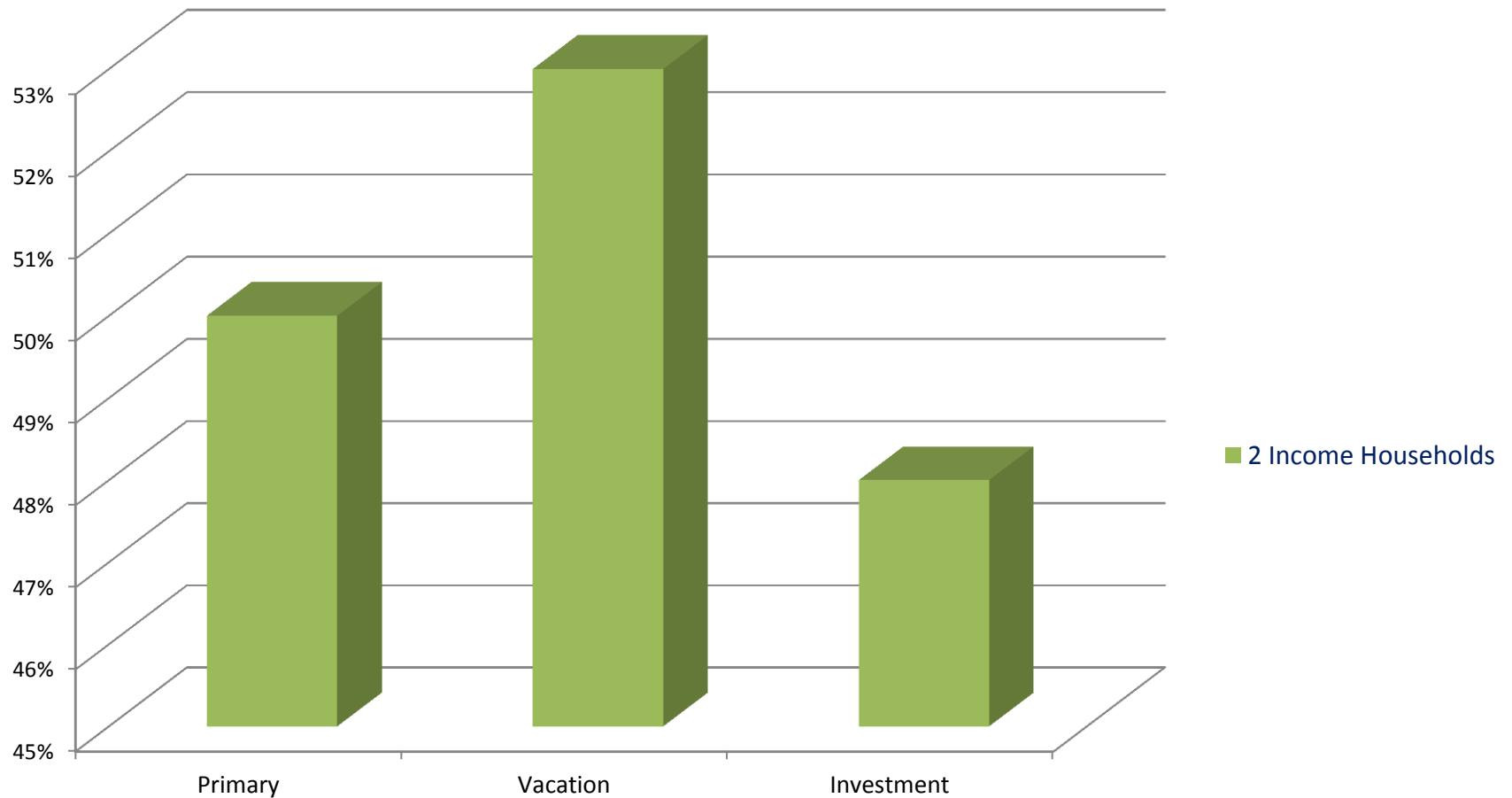
Source: 2011 NAR Survey of Investment/Vacation Home Buyers

Median Income of Investment/Vacation Home Buyers



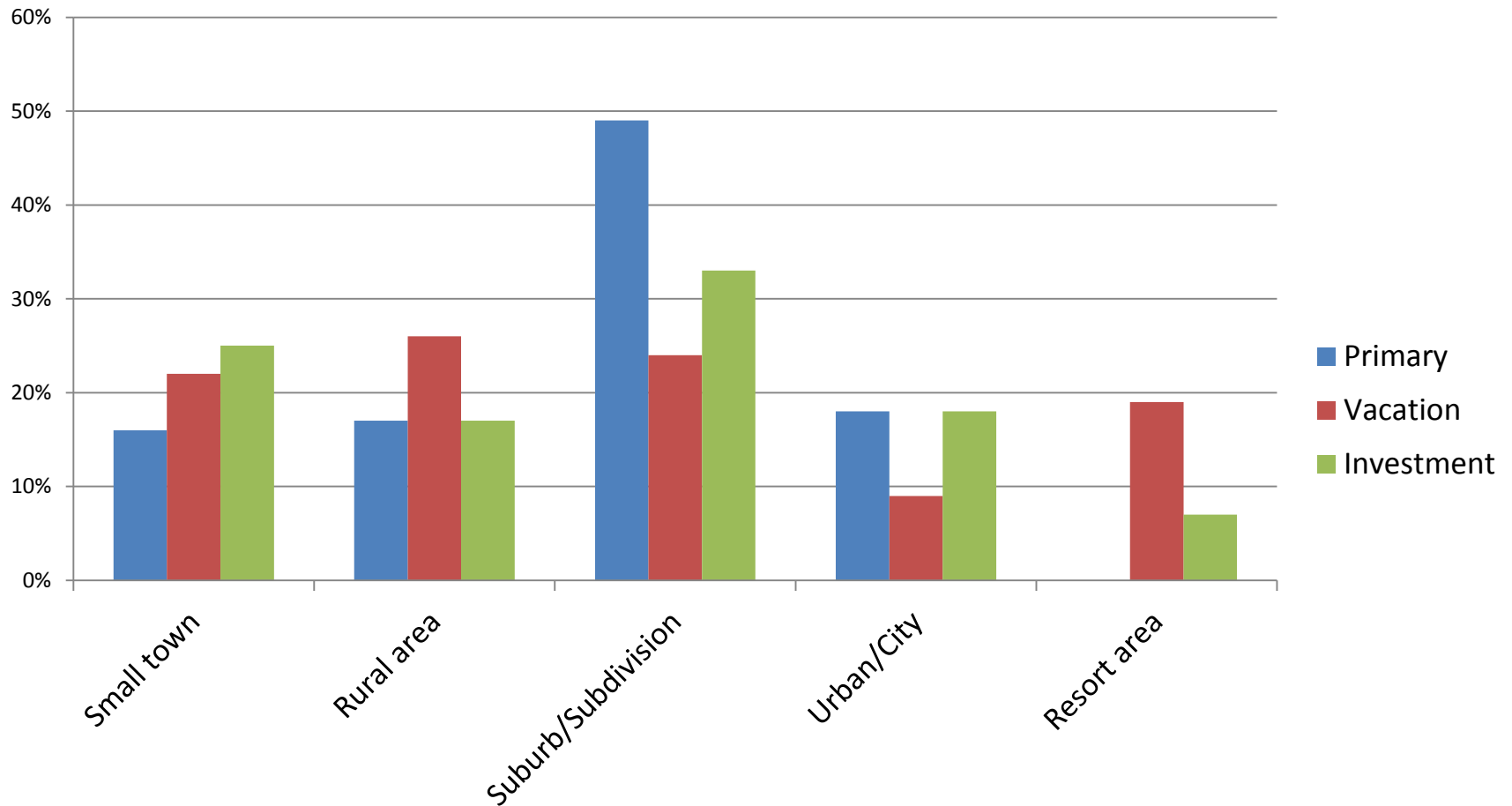
Source: 2011 NAR Survey of Investment/Vacation Home Buyers

Percentage of Two Income Households



Source: 2011 NAR Survey of Investment/Vacation Home Buyers

Where do they buy?



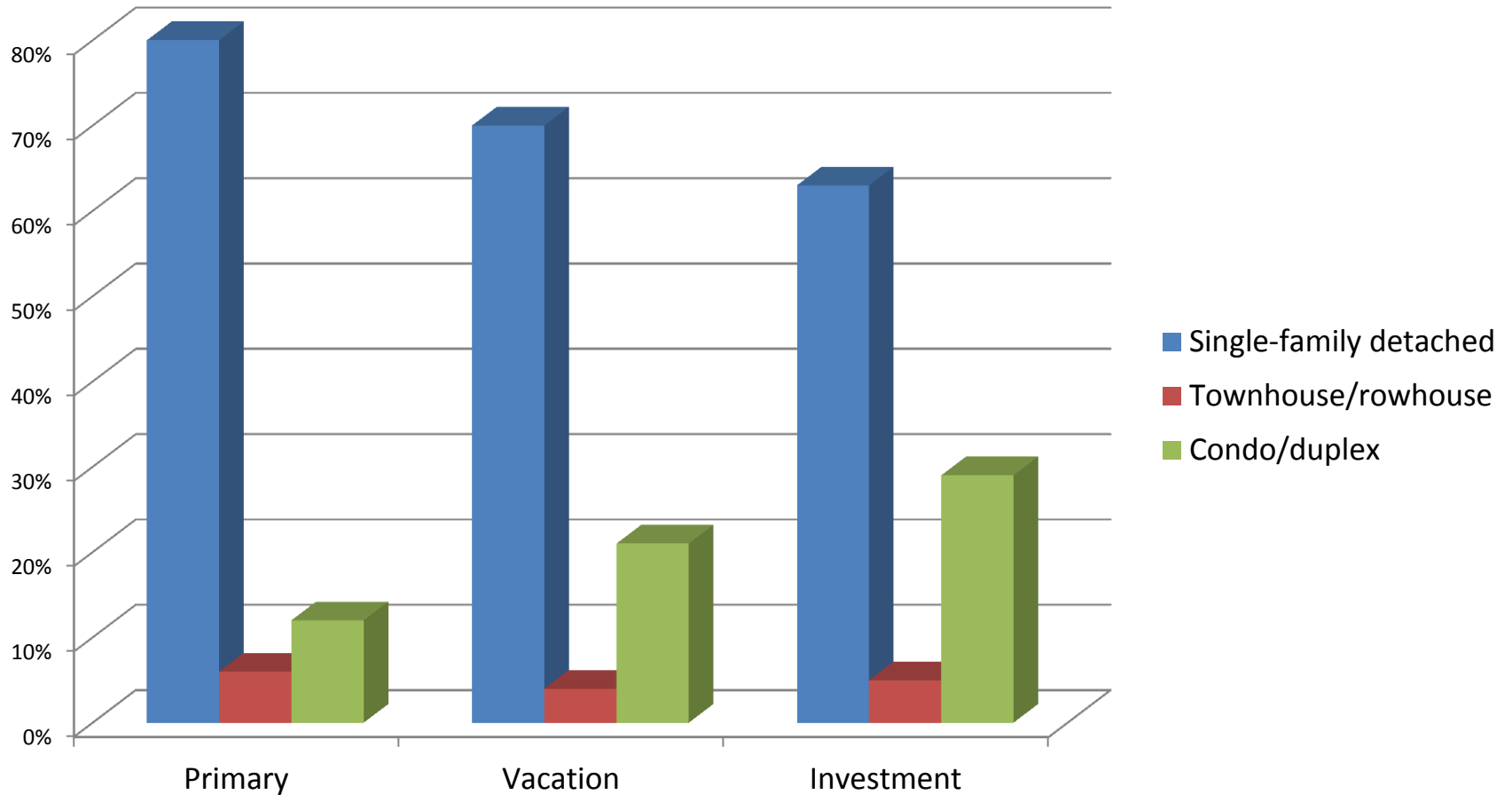
Source: 2011 NAR Survey of Investment/Vacation Home Buyers

How far away did they buy?

Median distance from home:

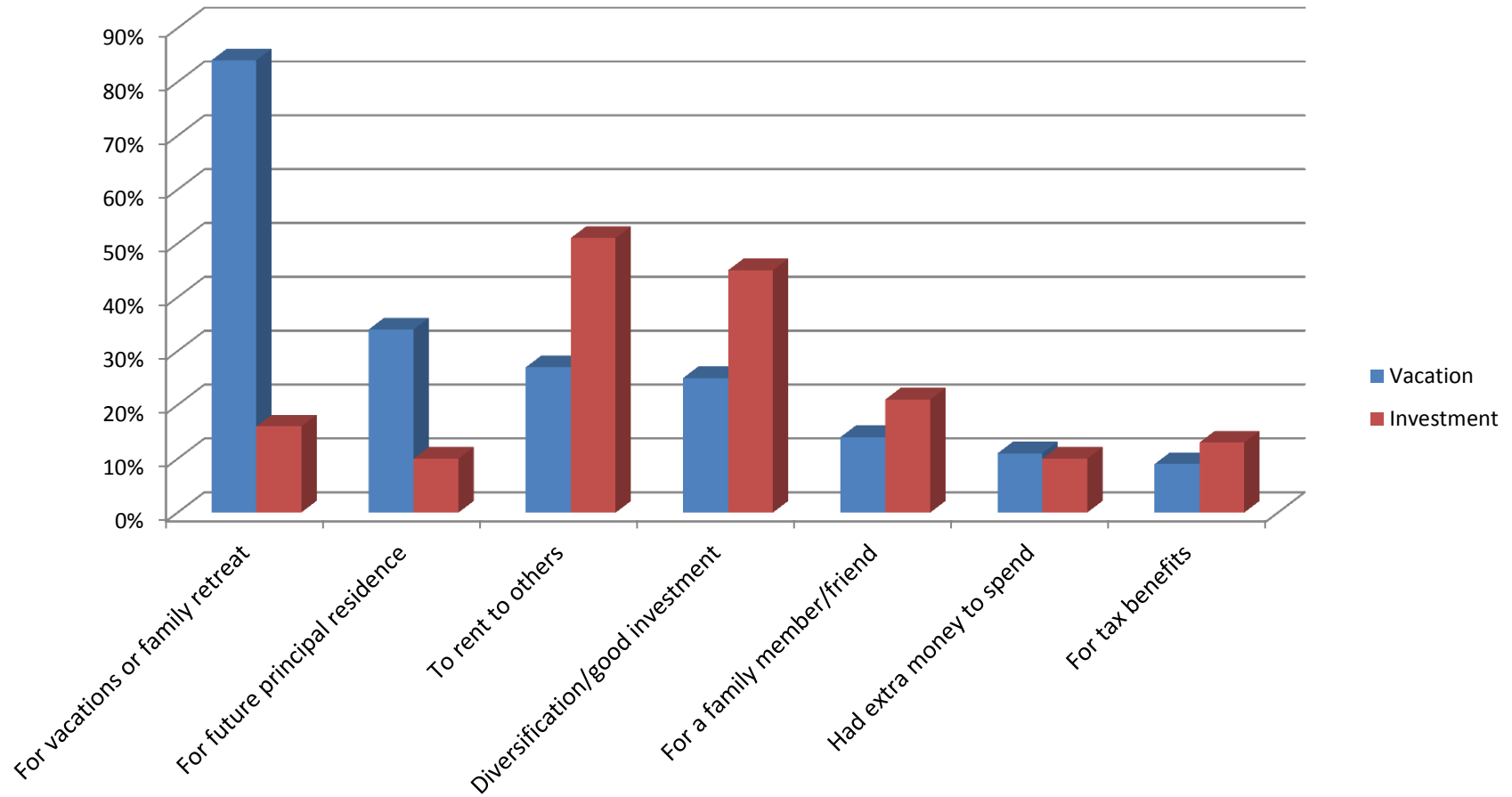
- Vacation home: 375 miles
- Investment property: 19 miles

What do they buy?



Source: 2011 NAR Survey of Investment/Vacation Home Buyers

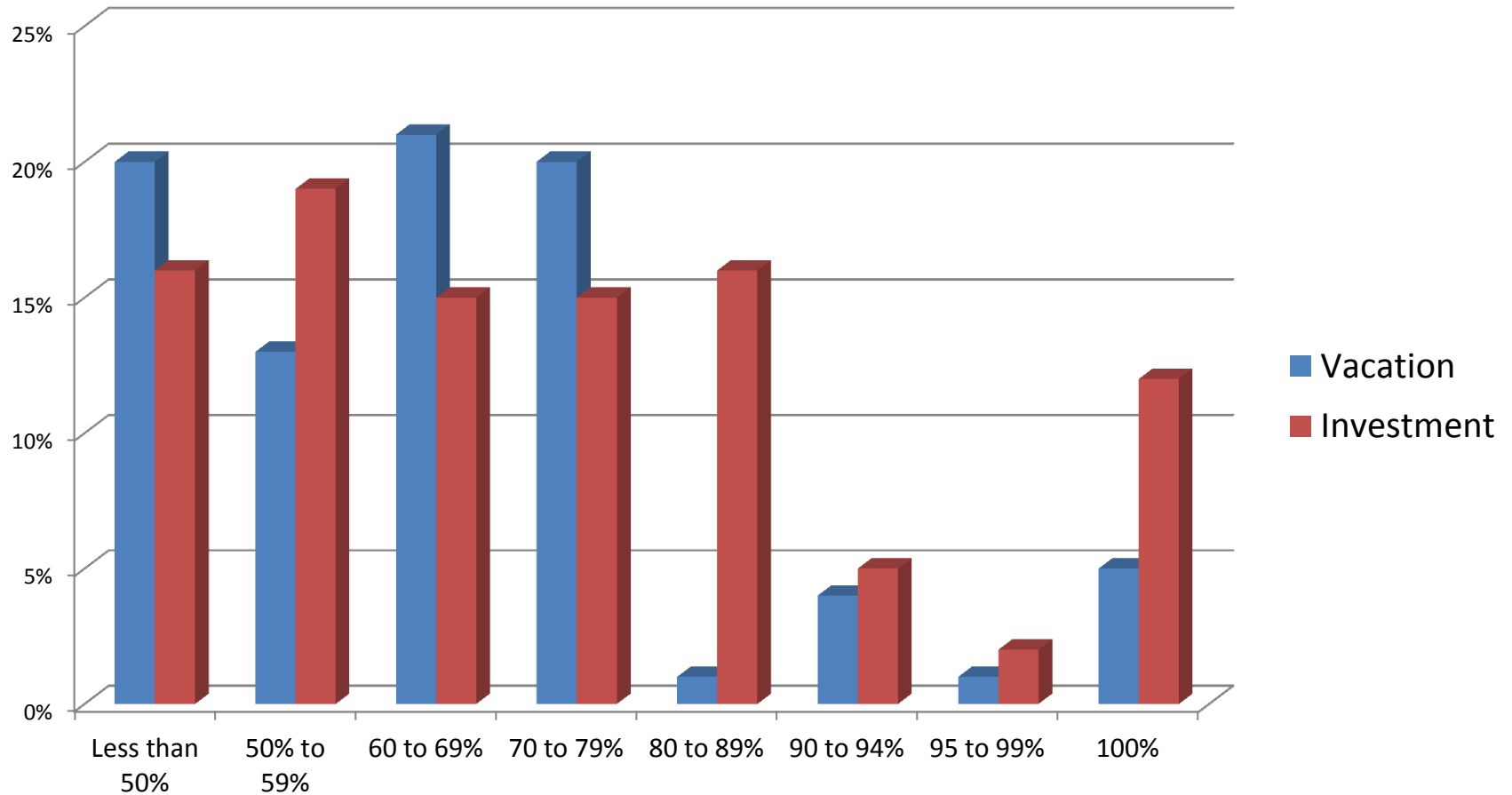
Why did they buy?



Source: 2011 NAR Survey of Investment/Vacation Home Buyers

How did they buy?

Percentage of Purchase that was Financed



Source: 2011 NAR Survey of Investment/Vacation Home Buyers

Vacation Home / Investment Properties

Purchase Considerations:

- What is the purpose of the purchase?
- What's the expected time frame?
- How does the property fit into my portfolio?
- How will I finance the property?
- Who will manage/maintain/rent the property?

Mortgage financing

The mortgage market has “tightened up” since the downturn began.

Vacation Homes:

- 20% down payment
- Rates:

4% up to \$417,000

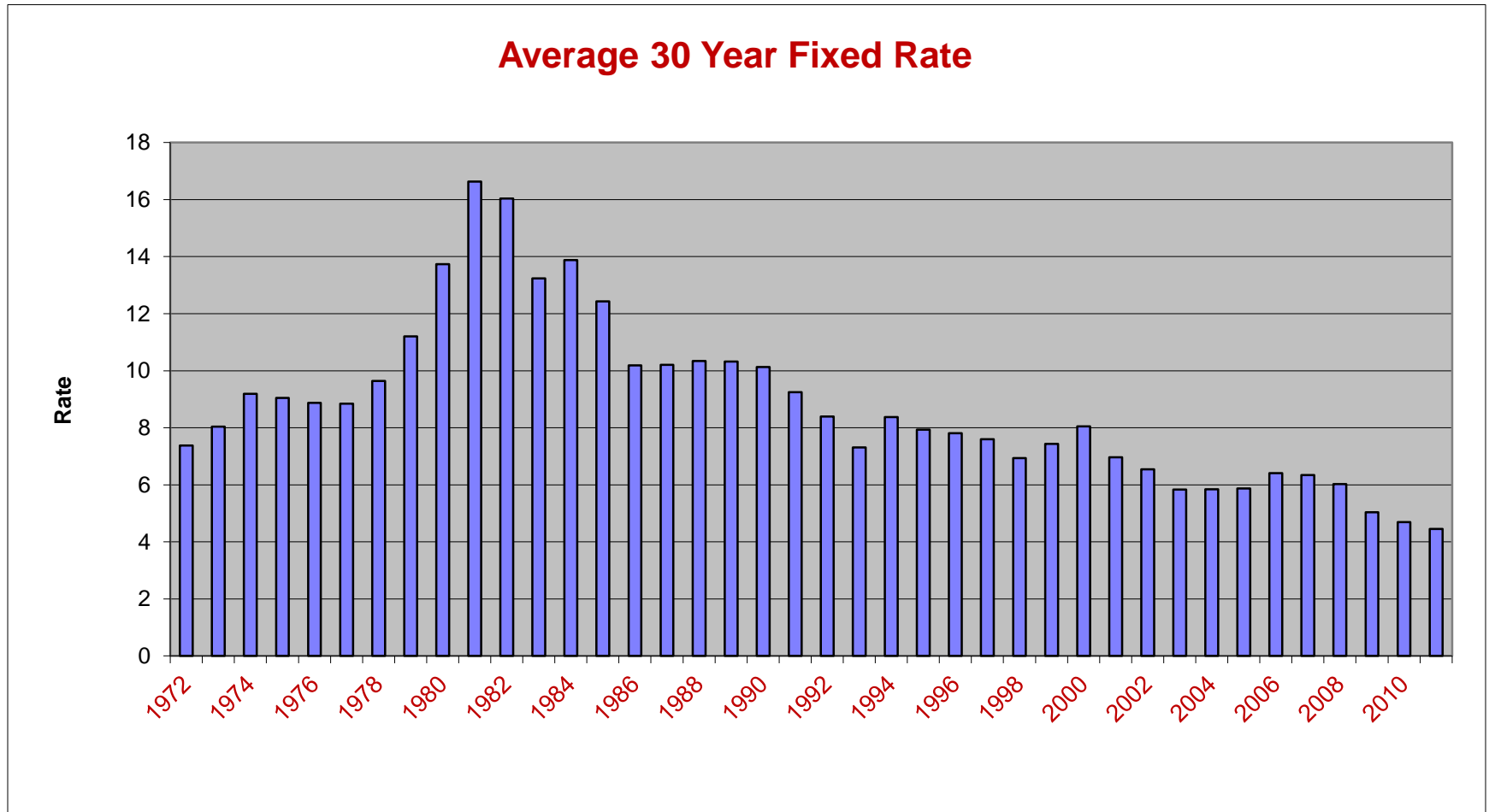
4.75% over \$417,000

Investment Properties:

- 25% down payment
- Rates:

About 4.75% and up

Average Conforming 30 Year Fixed Rate Mortgage



Source: Freddie Mac

Individual Ownership

Pros:

- Personal control of the property
- Property can be gifted under gift tax exemption
- Avoids NJ Bulk Sales Tax requirements upon sale (exception: multiple unmarried individuals)
- Easier to obtain financing as a first or second home
- File simple personal tax return

Cons:

- Personally liable for loss due to injury to persons or property
- All prior or future judgments in your name attach to the property
- Considered a personal asset for all purposes including Medicaid if care needed

Source: Cory J. Gilman, Esquire
Josephson, Wilkinson, & Gilman, P.A

LLC Ownership

Pros:

- Personal protection from liability for loss due to injury to persons or property
- No personal judgments in your name attach to the property.
(Judgments against the LLC would attach to the property)
- Property itself not a personal asset and not attachable for Medicaid if care needed.
(Share in LLC is considered an asset of value but property itself remains un-liable)
- Can take various deductions relating to operating a business

Cons:

- If multi member LLC, no direct control over property
- Only share in LLC can be gifted, not property itself
- No property tax deductions
- NJ Bulk Sale Tax requirements apply on sale
- More difficult to obtain financing
- Must file business tax return and file annual reports to state

Source: Cory J. Gilman, Esquire
Josephson, Wilkinson, & Gilman, P.A

The typical property is individually titled, with sufficient liability coverage, usually including an umbrella policy.

Rentals

- About 50% of purchases in our local market become rental properties
- Rental income/return varies greatly depending upon the location, type, size, and condition of property.
- Investment properties in some locations may be “positive cash flow”
- Vacation homes are sometimes rented for two weeks (tax free)

Tax Treatment*

(during ownership)

Second homes/vacation properties

- Mortgage interest & property taxes are deductible
- Can be rented for up to two weeks tax free

Investment properties

- Operating/maintenance expenses offset rental income
- Profits are taxable
- Losses can offset other income, subject to restrictions
- Unused losses can be carried forward

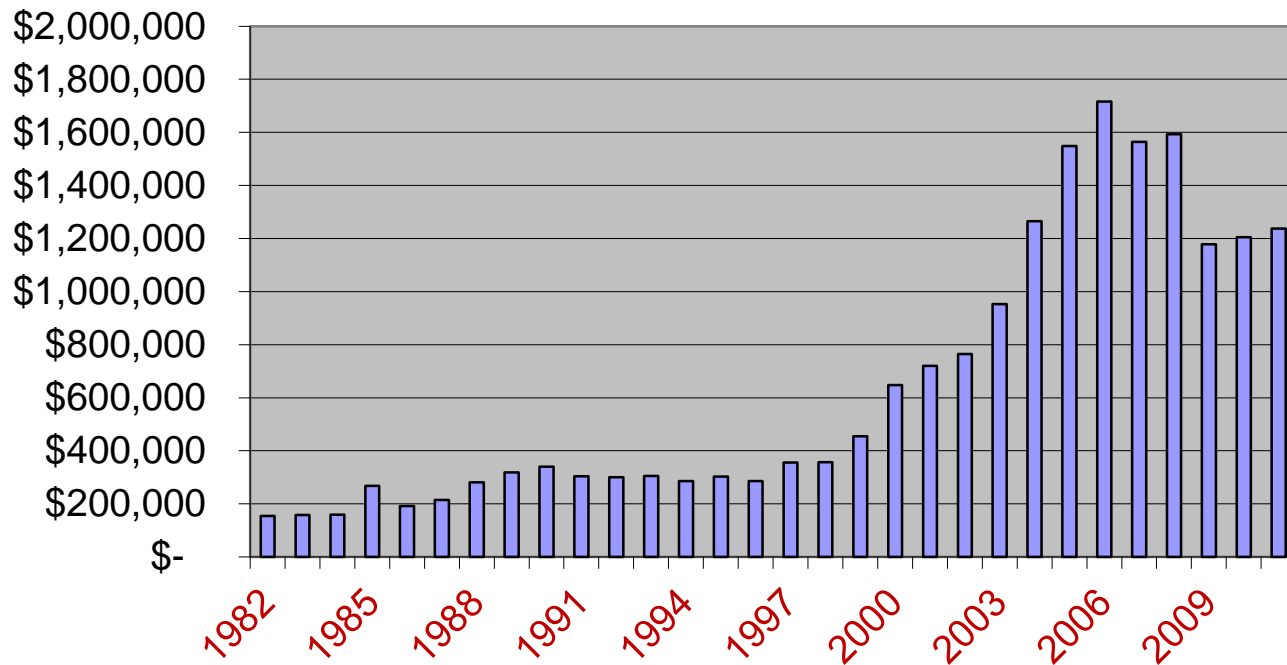
Source: James Rogers, Haefele Flanagan

**Always consult with your financial advisor or accountant about your personal situation, and current tax rules*

Long Term Price History

Average Sale Price 1982 - 2011

Avalon, Stone Harbor, Avalon Manor, Stone Harbor Manor



Source: Cape May County MLS

What do I do when I'm done with the property?

- Sell it
- Leave it to my kids
- 1031 Exchange

Vacation Home / Investment Properties Sale Considerations:

- What is the cost basis / anticipated capital gain?
- What are the costs necessary to sell the property?
- What is the expected time required to sell the property?
- In what calendar year / tax year will it be sold?
- What do I want to do with the net proceeds of the sale?
- What would I like to accomplish?

Sell the property

- Pros:

- Make use of the equity for other goals
- Relief from the burden of owning the property

- Cons:

- Capital gains tax due upon sale
- No more vacation home usage or rental income

Tax Treatment*

(at time of sale)

Second homes/vacation properties

- Subject to capital gains tax

Investment property

- Subject to capital gains tax and depreciation recapture
- IRS Section 1031 Tax Deferred Exchange may be utilized to defer taxes

Source: James Rogers, Haefele Flanagan

**Always consult with your financial advisor or accountant about your personal situation, and current tax rules*

Leave it to my kids

- **Pros:**
 - Build a family legacy
 - Stepped up basis for heirs upon owner's death
- **Cons:**
 - Kids may not want it
 - Kids may not be able to afford it
 - Some want it and can't afford it
 - Some can afford it and don't want it

Who Gets the Vacation Home?

- “Distance and lack of money are the big reasons a family member might want out...”

Source: Wall Street Journal, January 7, 2012

IRS Section 1031 Tax Deferred Exchange

- **Pros:**
 - Tax on capital gain is deferred
 - Full amount of net proceeds can be used for purchase of replacement property
 - “Defer, defer, defer, die!”
- **Cons:**
 - Property must have been held for “investment purposes” (no vacation homes)
 - Strict timeline requirements for execution of exchange
 - Must purchase a replacement property of equal or greater expense to avoid tax

Source: Ray Poling, Realtex 1031 Tax Deferred Exchange Intermediary Services

The question we're always asked...

“Is it a good time to buy?”

Buyer's Outlook:

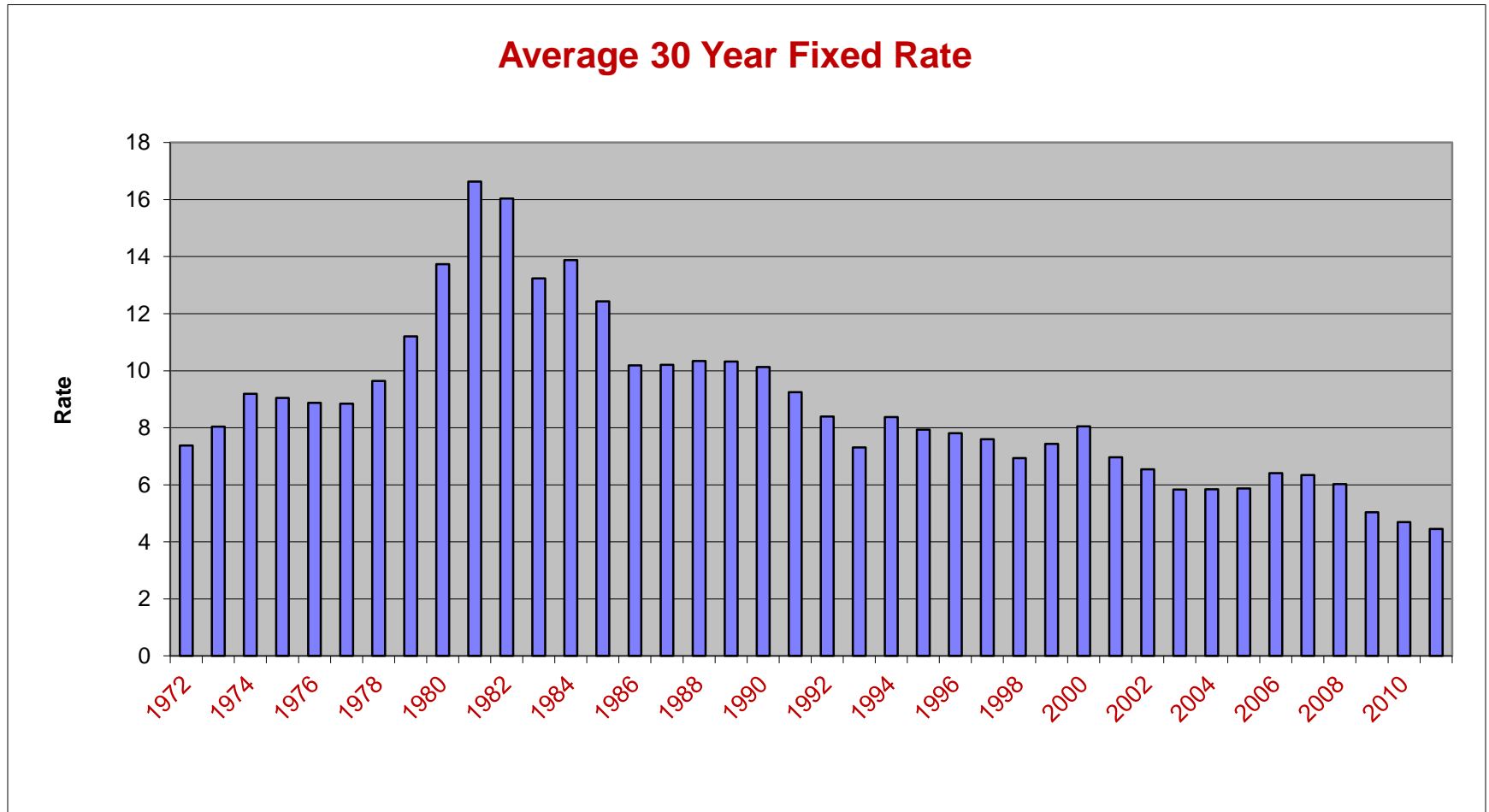
80% of vacation home buyers

and 77% of investment property buyers

think it's a good time to purchase real estate

Source: 2011 NAR Survey of Investment/Vacation Home Buyers

Average Conforming 30 Year Fixed Rate Mortgage

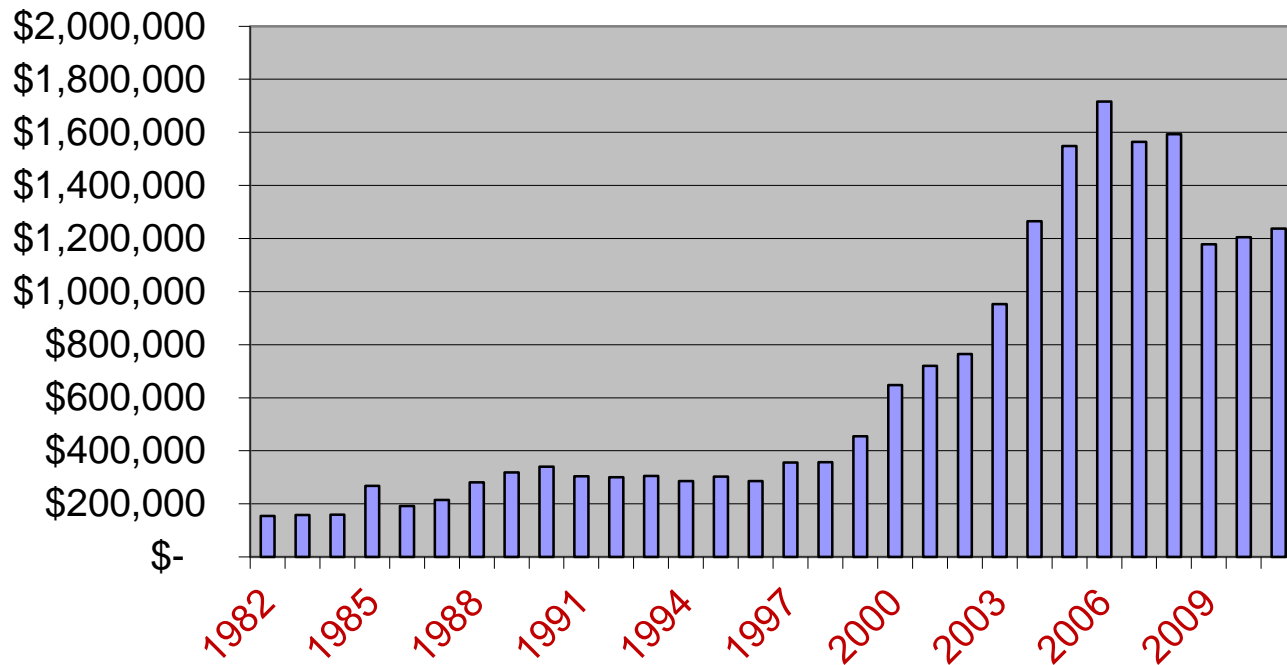


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