PRESERVING YOUR INVESTMENT IN YOUR COLLECTIBLE CAR
"A 1031 EXCHANGE CAN DEFER CAPITAL GAIN TAXES"

O.K., so you bought that sweet XKE some years ago just knowing that it would become a rare collectible. Well, it has: according to www.NADAguides.com, the average increase in collectible car values from February 2004 to February 2008 was 36 percent, which is over double the S&P 500 Index for the same timeframe. Collectible cars valued over $125,000 appreciated the highest amount of any pricing category, a sizeable 47%. Appreciation of this magnitude is good news for car collectors. It may seem like a good thing to sell your gem at today's market value . . . that is, until the tax man cometh.

Gains realized on the sale of collectibles are taxed at a special capital gains rate of 28%. For collectibles held for less than one year, the short-term rate is equal to the seller's marginal tax rate on ordinary income. To learn more about these tax rates, see the article, Understand the Impact of Tax Treatment: Ordinary Income vs. Capital Gain.

PAY TAXES AT 28% OR 0% WITH A 1031 EXCHANGE?

With high market prices available for collectible cars (and other collectibles such as paintings and photographs), long term investors are discovering that the taxes due on a sale can be substantial. To avoid the tax on the sale of a collectible that has been held for investment, the investor may complete a tax deferred exchange under Internal Revenue Code Section 1031. Real estate investors and business owners have been taking advantage of the tax deferral afforded by Section 1031 since 1921, but investors in collectibles have been slower to utilize an exchange to defer taxes. There is a growing realization among savvy investors, however, that they can reinvest all the profits resulting from the sale of a collectible tax deferred instead of paying capital gain taxes.

The "like-kind" requirements for personal property are much narrower than the standards applicable to real property. Moreover, an investor must establish to the satisfaction of the IRS that the collectible exchanged under Section 1031 was held primarily for investment or for use in a trade or business and not for personal enjoyment. This can be trickier with collectibles that may be purchased, at least in part, for the owner's personal enjoyment. For more information on the property that can be exchanged under Section 1031, see the article Personal Property Exchanges: Planes, Trains and Automobiles.

To defer paying capital gain taxes, the investor's replacement collectible car should be equal or greater in value than the car being sold in the exchange. In addition, all of the net proceeds (after paying commissions and closing costs) must be reinvested in qualifying replacement property if there is to be full tax deferral. Finally, an investor has up to 180 calendar days to complete the acquisition of the replacement car. It is important to work closely with a reputable qualified intermediary to facilitate the tax deferred exchange. Ordinarily, the qualified intermediary will prepare the necessary exchange documents and hold the sale proceeds securely in a separate account until they are disbursed on behalf of the investor to acquire the replacement car. We can help you understand your options, so give us a call to learn more.

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National Headquarters

800-282-1031

Eastern Region Office

866-394-1031

apiexchange.com

info@apiexchange.com

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