



Full Diagnostic Report

Prepared for: Marcus Levinson

Client Profile

Field	Value
Income	\$320,000
Filing Status	Married Filing Jointly
Entity Type	Sole Proprietorship (Disregarded Entity)
Real Estate Agent	<input checked="" type="checkbox"/> Yes
K-1 Income	<input checked="" type="checkbox"/> None
LTR Properties	3
Flips (Past 12 Months)	2
Material Participation	820 Hours
Grouping Election Filed	<input checked="" type="checkbox"/> No
Augusta Rule Used	<input checked="" type="checkbox"/> No
Vehicle Deduction	<input checked="" type="checkbox"/> Yes
Home Office Deduction	<input checked="" type="checkbox"/> Yes
Passive Losses Carried	\$25,000
Bookkeeping System	Basic Spreadsheet
Contractors Used	<input checked="" type="checkbox"/> Yes
Net Profit per Flip	~\$42,000 each



Executive Summary

Marcus is a real estate investor earning \$320K annually through a Sole Proprietorship. He owns 3 long-term rental properties and flipped 2 properties last year. He is a licensed real estate agent who logged 820 hours of material participation.

While he likely qualifies for **Real Estate Professional Status (REPS)** under IRC §469(c)(7), major execution gaps exist:

- ❌ No grouping election (Reg. §1.469-4)
- ❌ No time logs to substantiate REPS
- ❌ Augusta Rule not utilized
- ❌ Full SE tax exposure on flips via Schedule C
- ❌ No retirement deferral or entity planning

Total missed tax savings: \$30K–\$45K+ annually

REPS Qualification Analysis

Legal Tests for REPS (§469(c)(7)):

- ✅ **750-Hour Rule:** Client logged 820 hours – PASSED
- ✅ **More-Than-Half Rule:** No other job reported – PASSED
- ❌ **Material Participation per Activity:** AT RISK
Without a grouping election, each of the 3 rentals must individually pass material participation – unlikely without logs.

Case Law:

- *Bailey v. Comm., T.C. Memo 2001-296:* REPS denied despite hours because no grouping election.
- *Moss v. Comm., T.C. Memo 2014-8:* Court rejected REPS due to lack of contemporaneous time logs.

Conclusion:

Marcus is **at high risk of REPS denial** unless a **late grouping election is filed** and logs are reconstructed.



Passive Loss Utilization

- \$25,000 in passive losses remain suspended.
- Unlocking REPS allows **full deduction** against active income.
- Without it, losses roll forward indefinitely with no short-term benefit.

Missed Deductions & Elections

Strategy	Status	Comment
Grouping Election (§1.469-4)	✗	Not filed. Required for REPS on multiple properties.
Augusta Rule (§280A(g))	✗	Missed opportunity for ~\$4–6K tax-free rental income.
Vehicle Deduction (§274(d))	✓	Claimed. Needs substantiating mileage logs to hold up to audit.
Home Office Deduction	✓	Claimed. Must not be duplicated elsewhere (e.g., Augusta overlap).
Solo 401(k) or SEP IRA	✗	No contributions reported. Opportunity to defer \$22–66K annually.

Strategic Action Plan

1. REPS Defense

- File **late grouping election** (Rev. Proc. 2010-13)
- Create compliant time logs:
 - Activity
 - Date
 - Property
 - Hours
- Use *Moss v. Comm.* format to prevent rejection.



2. Flipping Entity Optimization

- Flips taxed on **Schedule C** = full SE tax
- Recommend forming **S-Corp**:
 - W-2 salary + distributions = reduce SE tax
 - Enhances audit protection and liability shield

3. Retirement Planning

- Fund **Solo 401(k)** using RE agent income
- Potential \$66K+ tax deferral annually
- Leverage to optimize AGI and increase deductions

4. Augusta Rule Strategy

- Rent personal home to business for up to 14 days/year
- Use FMV rental (\$300–\$400/day) = **\$4,200–\$5,600 tax-free**

Audit Risk Matrix

Risk Area	Level	Legal Basis
No Grouping Election	🔴 HIGH	Reg. §1.469-4; <i>Bailey v. Comm.</i>
No Time Log	🟡 MODERATE	<i>Moss v. Comm.</i>
Flips on Schedule C	🟡 MODERATE	§1402 – triggers full SE tax
Mixed Income Buckets	🟡 MODERATE	RE Agent + flips without separation
Missed Augusta Strategy	✅ LOW	Not risky, just a missed opportunity



Proposed Tax Savings Summary

Strategy	Estimated Annual Savings	Notes
S-Corp Conversion	\$6,000–\$8,500	On ~\$84K flip income
Solo 401(k) Implementation	\$12,000–\$20,000	Based on RE Agent net income
REPS Activation	\$6,250	Unlock \$25K passive losses @ ~25% marginal rate
Augusta Rule	\$4,000–\$6,000	14-day tax-free rental of home
Vehicle Strategy	\$1,500–\$2,000	Mileage log to protect existing deduction
Home Office Optimization	\$1,200	Based on clarified % usage

Total Potential Benefit

Projection Type	Annual Savings
Conservative	\$30,950
Aggressive	\$44,950+

Final Summary

Marcus is **under-leveraged and structurally exposed**. With a grouping election, S-Corp setup, Augusta Rule usage, and proactive documentation, he can unlock over **\$30,000/year in tax savings**, reduce audit flags, and transform his tax profile from reactive to strategic.