1031 TAX-DEFERRED EXCHANGES

Section 1031 of the Internal Revenue Codes allows the deferral of federal gain on the sale of a business use or investment real property provided another business use or investment property is acquired. This often-overlooked tax strategy can help investors accomplish many short and long-term investment objectives:

- Immediate tax deferral
- Ability to acquire real estate with pre-tax dollars
- Long-term appreciation on tax deferral
- Estate Preservation (deferred gain may be forgiven upon death of taxpayer)
- Less management responsibility
- Greater selling and buyer power
- Increased income potential
- Relocation/expansion of business
- Diversification/consolidation of assets
- Conversion to primary residence and eventually qualify for primary residence exclusion

REQUIREMENTS OF A SUCCESSFUL 1031 EXCHANGE

1. The relinquished property and the replacement property must be held for business use or investment. Almost any kind of real estate can be exchanged through a 1031 exchange except a primary residence or a “flip.” There are special rules that must be met in order for a vacation home to qualify.
2. The new property must be identified within 45 days and acquired within 180 days of the closing of the old property. You are permitted to identify multiple properties using The Three Property Rule (identify up to three properties regardless of their combined fair market value) or the 200% Value Rule (if identifying four or more properties, their combined value must be 200% or less than the value of the relinquished property).
3. Legal title to the relinquished and replacement properties must be held in the same owner.
4. The replacement property must be of equal or greater value and equity than the relinquished property. A trade down in either equity or value is taxed dollar for dollar.
5. A Qualified Intermediary (QI) is needed to facilitate the transaction. The QI prepares all required exchange documentation, provides written reminders of time deadlines, coordinates details with all parties and holds exchange proceeds in exchange account until the replacement property is acquired.

10 STEPS TO TAX SAVINGS WITH A 1031 EXCHANGE

1. Sign Listing Agreement to sell relinquished property.
2. Sign Agreement of Sale with Buyer.
3. Retain Qualified Intermediary (QI).
4. QI prepares documents and provides closing agent with instructions to ensure closing documents the exchange properly.
5. Closing takes place and proceeds are forwarded to QI and placed into exchange account.
6. The 45-Day Identification Period and 180-Exchange Period begin.
7. Identify replacement properties to QI. Typically the QI will provide a form letter and instructions to keep this step of the exchange easy.
8. Sign Agreement of Sale for replacement property and use exchange proceeds for earnest money deposit.
9. QI provides closing/escrow officer with instructions and transfers exchange funds.
10. Replacement property is acquired and the exchange is complete.