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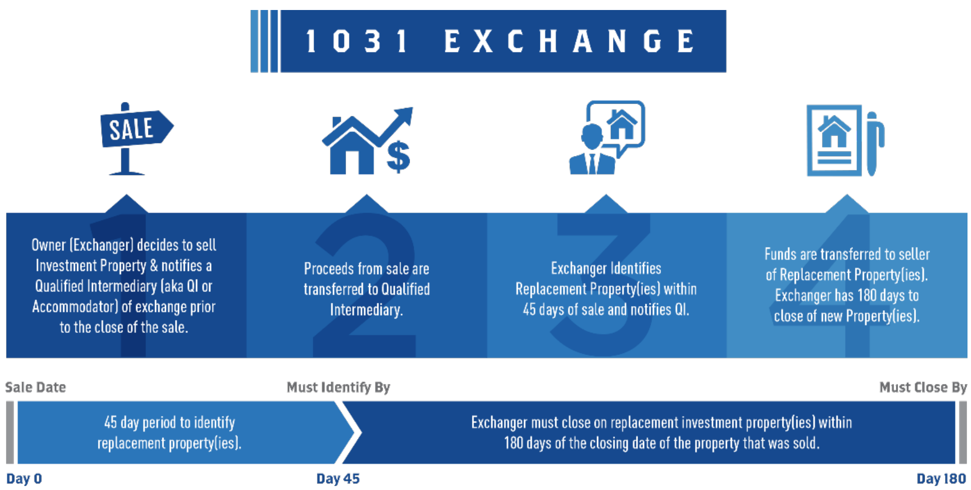
§ 1031 Tax Exchange

With significant gains in real estate over the past 10 years, and interest rates at historical lows, diversifying real estate holdings via a 1031 exchange remains an attractive strategy for many investors. Some of the most suitable properties for a 1031 exchange are: single family rental homes requiring significant time and expenditure on the part of the owner, business owners who own real estate occupied by their current (or former) company, properties with below-average cash flow, and properties or raw land in desirable locations that have appreciated significantly over time.

What is a 1031 Exchange?

The Internal Revenue Code (IRC) provides that a taxpayer may sell real property and defer payment of capital gains tax if that taxpayer uses the proceeds to acquire a like kind replacement asset.

IRC § 1031 provides that neither gain nor loss is recognized if property held for investment or productive use in a trade or business is exchanged for property held for investment or productive use in a trade or business.



Why Exchange?

- Capital gains tax is significant;
- Reinvestment into replacement property allows taxpayer to leverage dollars that would otherwise be spent on taxes;
- Allows for non-income producing property to be replaced with income producing property; and
- Allows taxpayer to diversify portfolio and minimize risk.

3 Requirements to Defer Capital Gains Tax under § 1031

(1) The property sold and the property received must be held for productive use in a trade or business or for investment (and the owner cannot change);
(2) The property sold and the property received must be of "like-kind", although it is permissible to exchange a few properties for one (or vice versa) or residential for commercial (or vice versa); and

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(3) There must be an "exchange" as distinguished from a "purchase and sale", which involves using a Qualified Intermediary (QI) to hold funds from the relinquished property sale and disbursed at the closing on the replacement property (the taxpayer may not take receipt of funds).

Deadlines

- The Exchanger must identify replacement property with **45 calendar days** after the close of the relinquished property.
- Within **180 calendar days** from the sale of the relinquished property, or the Exchanger's tax filing date, whichever is earlier, the Exchanger must acquire like-kind replacement property (as identified above).

Identification Methods (45 days)

There are three methods for replacement property identification, completed within 45 days after the sale of the relinquished property, which limit the number of properties the Exchanger may identify. Below are the two most common options:

Options	Description
3 Property Rule	Three properties are identified, no matter what the fair market value.
200% Rule	Any number of properties as long as the aggregate FMV does not exceed 200% (2x) the FMV of all the relinquished properties.

Finding a Replacement Property

When it comes to identifying a replacement property for your 1031 exchange, there is a range of options from self-managed, direct investments (think single-family rentals) to national funds that pool investor capital.

- **Self-managed:** Identifying a replacement property on your own is always an option. The downside is that you will likely have to continue to manage the property or may sacrifice income by hiring a management company. Many clients that we work with on 1031 exchanges have a desire to stop the day-to-day involvement of managing their real estate, and instead simply want to collect rent, so continuing to self-manage is not the best option.
- **Delaware Statutory Trust (DST) / Exchange Funds:** DSTs and Exchange Funds are "pre-packaged" real estate investments for fractional ownership in real estate, meaning that the property has already been acquired prior to the 1031 exchanger's investment. These funds offer low minimum investments and are readily available, so timing is not a concern, but often come with higher fees and, as a result, less favorable returns.
- **Limited Partnership (TIC):** Through our relationships in real estate, we have identified a pipeline of sponsors with suitable replacement properties for 1031 exchange investors. By making direct investments alongside experienced real estate professionals, we can help our clients negotiate better structures and deal terms for their investments.