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Agenda

Introduction and basics

Purpose of Sec. 1031 exchanges

Deeper dive

Types of exchanges

Role of Q.I.

Basic guidelines

Common pitfalls

How can CLA and IPX help





Definition

IRC Section 1031(a)(1):

No gain or loss shall be recognized on the exchange of real property held for productive use in a trade or business or for investment if such real property is exchanged solely for real property of like kind which is to be held either for productive use in a trade or business or for investment





What Does That Mean for You?

A taxable sale may include such taxes as:

Federal capital gains tax
Federal tax on depreciation recapture
Federal net investment income tax
State capital gains tax

Potential to defer both federal and state taxes on property sale

Ability to invest more dollars into real estate





Basic 1031 Transaction Types

Forward

Sell your property then acquire the new

Reverse

Acquire the new property and then sell yours

Improvement

Construct improvements to property during 180-day period





Role of 1031 Company / Qualified Intermediary

Safeguard funds

Generate 1031 documentation

Guide exchanger, broker, and counsel through process





Basic Guidelines in a 1031 Exchange









Equal or greater

- Reinvest all sale proceeds
- Replace all debt

Taxpayer continuity

Same taxpayer rule

Like-kind

- Investment or business use requirement
- Domestic for domestic
- Foreign for foreign

Time periods

- 45-day identification period
- 180-day exchange period





Breaking Down the Numbers

- The "napkin test"
- For 100% gain deferral, taxpayer must:
 - Trade up or equal in property value
 - Trade up or equal in equity



Napkin Test – Example 1

Equal value and greater equity

Relino	uished	Property
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Replacement Property

Value

\$1,000,000

Value:

\$1,000,000

Loan:

\$ 500,000

Loan:

\$ 400,000

Equity:

\$ 500,000

Equity:

\$ 600,000

Note: in this transaction, there is \$100k of debt boot but is offset by \$100k of additional cash



Napkin Test – Example 2

Lower value and equal equity

Relino	uished	Property
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Replacement Property

Value \$1,000,000

Value:

\$800,000

Loan:

\$ 500,000

Loan:

\$300,000

Equity:

\$ 500,000

Equity:

\$500,000

Note: in this transaction, there is \$200k of taxable boot despite 100% equity reinvestment



Same Taxpayer Requirement

Same taxpayer who transfers relinquished property must acquire replacement property

Favorable exceptions:

- Disregarded single-member LLC and the sole member
- Grantor/Revocable Trust Disregarded entity
- If taxpayer passes during exchange, their estate may complete the exchange, Rev. Rul. 64-161



What Properties Types May Qualify?

- Retail, office, and industrial
- Residential
- TIC and DST interests
- Raw land
- Long-term lease
- Mineral, air, oil, and gas rights
- Perpetual easements
 - Vacation rentals





What Properties Types Typically Don't Qualify?







Property Identification Rules 200% 95%

Three Property Rule

The Exchanger may identify up to three properties of any value.

200% Rule

The Exchanger may identify more than three properties if the total fair market value of what is identified does not exceed 200% of the fair market value of what they sold

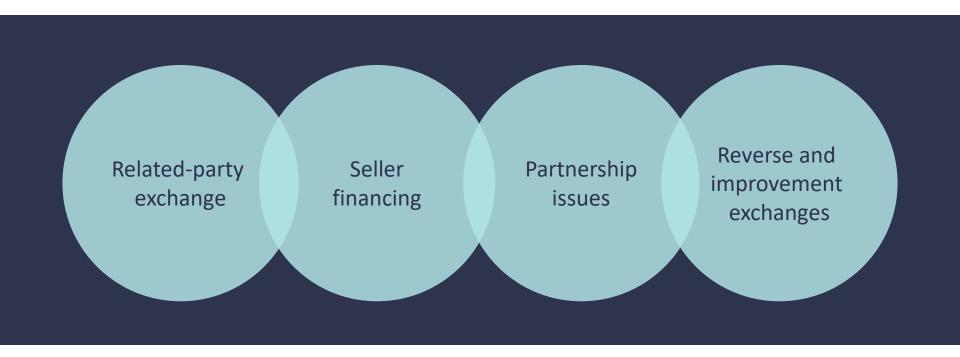
95% Exception

If the Exchanger identifies properties in excess of both Rule 1 and Rule 2, then the Exchanger must acquire at least 95% of the value of all properties identified.





Common 1031 Pitfalls







Pitfalls: Related-Party Exchange

- Who may be deemed a related party?
 - Siblings, spouse, ancestor, lineal descendants
 - Corporations and/or partnerships with common control
- Why is it important?
 - Related party transactions can be denied 1031 treatment
- Permissible related party transactions
 - Related party swap
 - Both parties engaging in an exchange
 - Transactions with no basis shifting



Pitfalls: Seller Financing

- Exchanger has cash prior to closing
- Exchanger does not have cash prior to closing
- Partial exchange

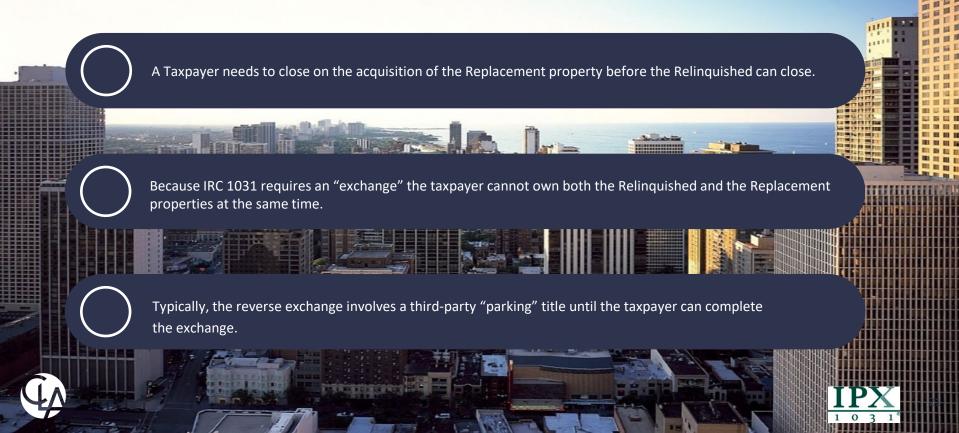


Pitfalls: Partnership Transactions

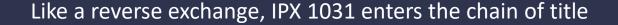
- Partnership is selling property but partners have different goals
- Possible planning opportunities:
 - Buyout exiting partner
 - Distribute undivided interest to exiting partner
 - Drop and swap
 - Swap and drop



What Is a Reverse Exchange?



Built to Suit Exchange



Holds title until the improvements are completed

45 days to notify us of the improvements you're going to make

180 days to complete the improvements



Polling Question

Would you like someone from CLA to contact you regarding Section 1031 consulting and/or compliance and reporting?

- Yes
- Not at this time



Thank you for joining us!

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