

# Strategic 1031 Exchange Advisors

## OUR BUSINESS PRINCIPALS

### SECURITY

Industry-leading security measures that ensure exchange fund liquidity and principal protection

### KNOWLEDGE

Expert team of CPAs, MBAs, and attorneys that provide exchange guidance for forward, reverse, build-to-suit construction, leasehold, international, personal property, multi-asset, and other complex exchanges

### SERVICE

A significant value-adding resource with exceptional client service and innovative strategies that complement core business objectives

## STRATEGIC EXCHANGE ADVISORS



An Insight into:

## 1031 Exchange Fundamentals

Internal Revenue Code §1031 allows for the deferral of capital gains tax on the sale of qualified like-kind property. It also allows for the deferral of depreciation recapture and deferral of state taxes (where applicable). In some cases, the deferral can be indefinite, as the taxpayer will not recognize the capital gain until the replacement property is sold without the use of an exchange.

### *Defining “Like Kind” for Real Property*

Exchanges under Section 1031 of the Internal Revenue Code are often referred to as a “Like-Kind” Exchange due to the requirement that exchanged properties must be like-kind to one another. The like-kind requirement for real estate is broadly defined, thus allowing taxpayers to exchange, for example, residential rental property for raw land, or a retail shopping center for an office building. However, the like-kind application for personal property is much more narrowly defined, often requiring assets to be part of the same IRS General Asset Class.

### *Qualified Property*

In order to qualify for exchange treatment, property must be held for investment or used in a trade or business. Examples of property used in a trade or business might include heavy equipment in a construction company, tractor trailers used by a shipping company, or an industrial building owned and occupied by a manufacturing company. Determining whether an asset is held for investment requires a facts-and-circumstances analysis of how the asset is treated by the taxpayer. Investment real estate is typically depreciated by the taxpayer, and is not held primarily for personal use. Further, investment property is not purchased for immediate resale purposes -- such property is treated as inventory, and therefore, is excluded from exchange

treatment. Other property that does not qualify for exchange treatment includes stocks, bonds, debt instruments, partnership interests, and goodwill.

### *Exchange Timelines*

From the day the taxpayer sells property (the “Relinquished Property”), he or she has 45 days to identify potential property(s) for purchase (the “Replacement Property”). The taxpayer must take title to the Replacement Property within 180 days from the date property was relinquished. These deadlines are not extended in the event they should fall on a weekend or holiday. The only circumstance where an extension is available are instances where the taxpayer or property has been affected by a Presidentially declared disaster.

### *Target Exchange Values*

In order to defer 100% of the capital gain tax associated with a transaction, the taxpayer must purchase Replacement Property that equals or exceeds the Relinquished Property value. Any shortfall will result in the taxpayer realizing tax on the amount not reinvested. Additionally, the taxpayer must reinvest all of the cash from the Relinquished Property sale (the “cash boot”) and replace any debt that was relieved of at the time of sale (the “mortgage boot”). The mortgage boot may be replaced with new cash, new debt or any combination thereof. During the exchange cash boot must be held by the disinterested third-party facilitating the exchange, known as a Qualified Intermediary. It is imperative that the taxpayer not have actual or constructive receipt of the cash boot during the exchange.

Please contact Strategic 1031 Exchange Advisors with any exchange questions.