

Introduction to 1031 Exchanges

PRESENTED BY:

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 **Advocus** National 1031 Exchange, LLC™

Course Objectives

Gain an understanding of the mechanics of a 1031-Exchange

Identify the steps and time restrictions of a 1031 Exchange

Gain an understanding of the federal rules and requirements in a 1031 exchange

Be able to identify other types of exchanges

Taxation 101

Generally, all income is taxable, unless specifically exempted by law.

Even illegal income, such as stolen or embezzled funds, must be reported on Form 1040.



IRC § 1031 (a)(1)

“No gain or loss shall be recognized on the exchange of real property held for productive use in or 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 for productive use in a trade or business or for investment.”

Note that Section 1031 provides for deferral of taxes, not complete elimination.

Value of 1031 exchange

A 1031 Exchange allows the property owner to potentially defer four levels of taxation:

- Federal Capital Gain (15% to 20%)
- Tax on depreciation recapture (25%)
- State income taxes (up to 13.3%), if applicable
- Net Investment Income Tax (NIIT; 3.8%), if applicable

SALE		EXCHANGE	
Sale Price	\$900,000	Sale Price	\$900,000
Expenses	- \$80,000	Expenses	- \$80,000
Est. Taxes	- \$180,000	Est. Taxes	\$0
			
Net After Tax Proceeds	\$640,000	Gross Proceeds (1031 = tax deferral)	\$820,000

Sale VS. Exchange

Equal Or Greater Value



Replacement property(ies) must be of equal or greater value to exchange value of relinquished property



Exchange value determined by subtracting closing costs and broker's commissions from relinquished property(ies) value



Exchange value not used in acquiring replacement is “boot” and taxable



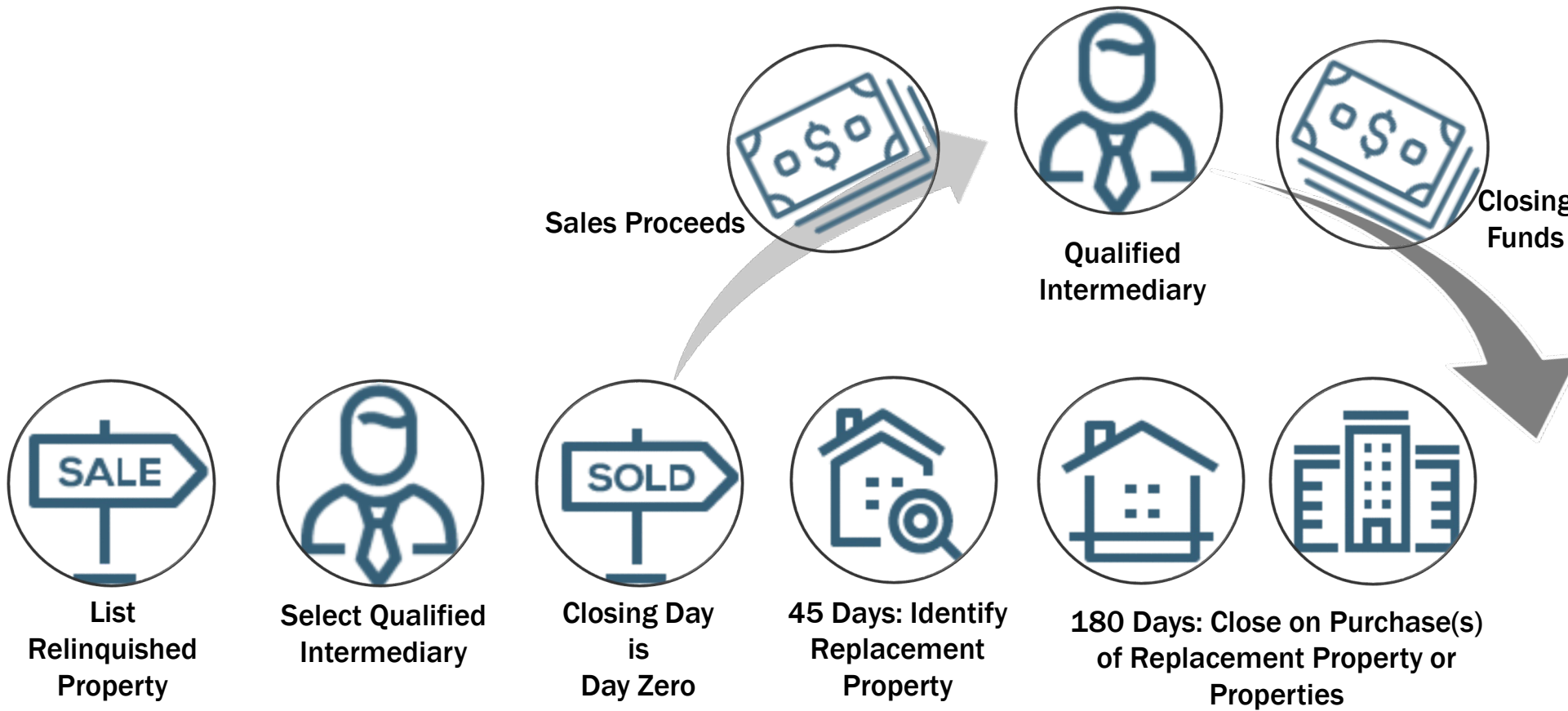
Equity AND debt must be replaced

What Is Considered “Like-kind” Property?

- Farmland
- Ranchland
- Hunting/Recreational Land
- Timberland
- Vacant Land
- Easements (Conservation and others)
- Mineral, oil, and gas rights
- Water and timber rights
- Wind and Solar farms
- Billboard sites
- Cell tower sites
- Other Property Types



The Process

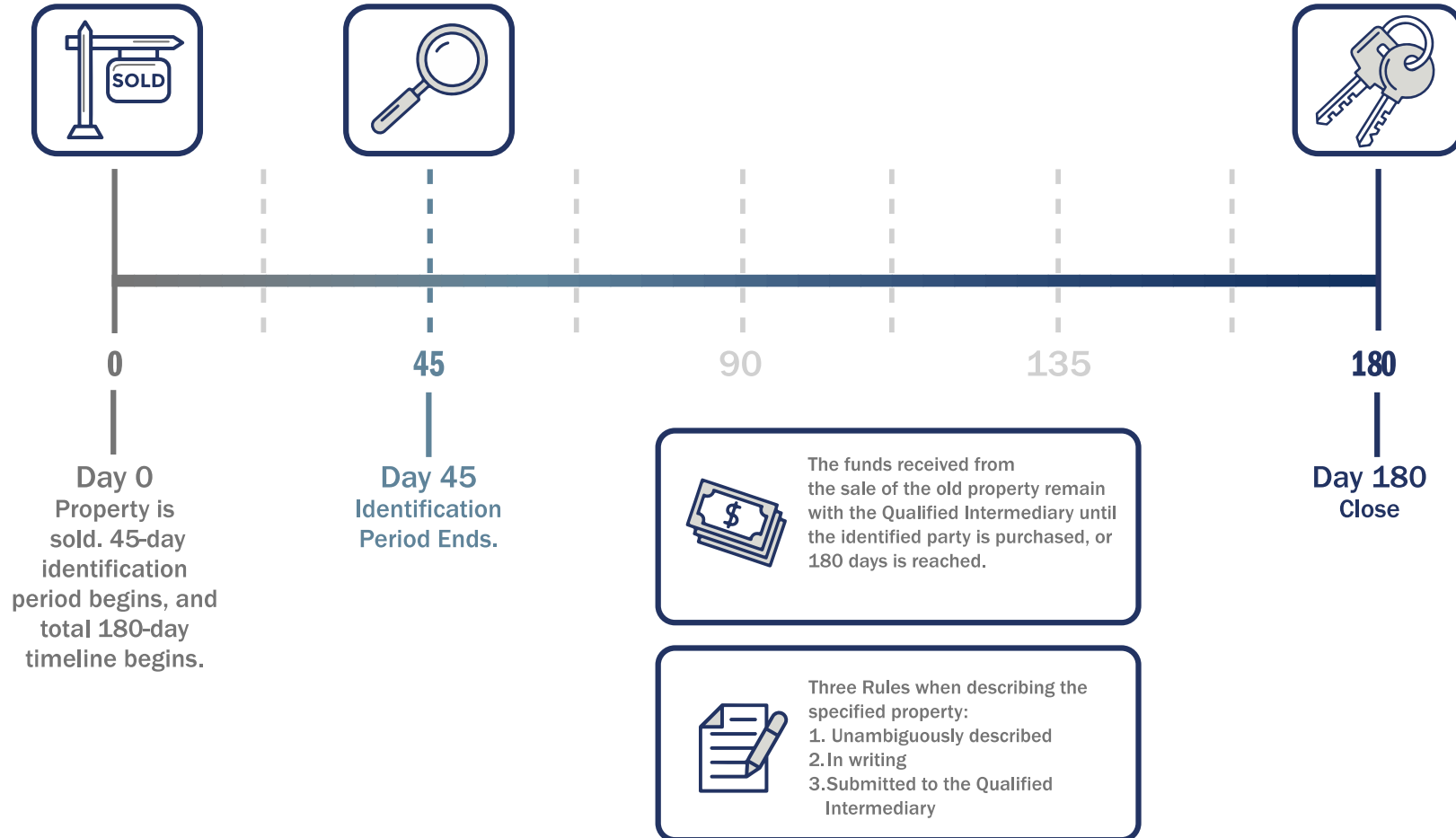


1031 Exchange Time Limits

1984 Congress amended Section 1031

- 45-day identification period
- 180-day exchange period runs concurrently
 - Or due date of tax return, whichever is earlier
- Calendar days, not business days
- No extensions
- Exchange starts on date of recording, or when burdens and benefits of ownership of relinquished property are transferred, whichever is first

The Timeline



Identification Requirements

Signed, and in writing

Delivered

- QI or seller of replacement property

Unambiguously described

- Legal description
- Street address
- Distinguishable name (e.g., Madison Square Garden)

May be revoked or amended, with same formality as above

Identification Rules

3

Property Rule

Up to 3 properties of any value

200%

Rule

Any number of properties (greater than three) so long as the value does not exceed 200% of the relinquished properties

95%

Rule

Exchanger violated first two rules, therefore must acquire at least 95% of the value of all properties identified

Section 1031 in a nutshell

To obtain complete deferral of capital gains taxes, the Exchanger should:

- Receive **nothing except like-kind** property
- Adhere to the 45-day and 180-day time limits
- Replacement property must be **equal or greater in value** to the relinquished property
- Must have **equal or greater equity** in the replacement property
- Must **replace the debt** (with cash or debt) on the replacement property
- Exchanger must avoid **constructive receipt** of exchange proceeds
 - Use a **Qualified Intermediary (QI)**

Exchanger can sell multiple properties, to consolidate into fewer properties

Exchanger can sell one property to diversify into many properties

Identification period – all replacement properties must be identified within 45 days of transfer of first relinquished property

Exchange period – all replacement properties must be acquired within 180 days of transfer of first relinquished property

Multiple Property Exchange

Same Taxpayer

Taxpayer that owns relinquished property MUST be same tax entity that acquired replacement property

- “Taxpayer” determined by tax return on which income/expenses/losses reported

Owner/titleholder may not be “taxpayer” for 1031 purposes

- Living trusts
- Single-member LLCs
- Illinois land trusts

Qualified Use

Business or investment

- Holding bare land to appreciate = “held for investment”

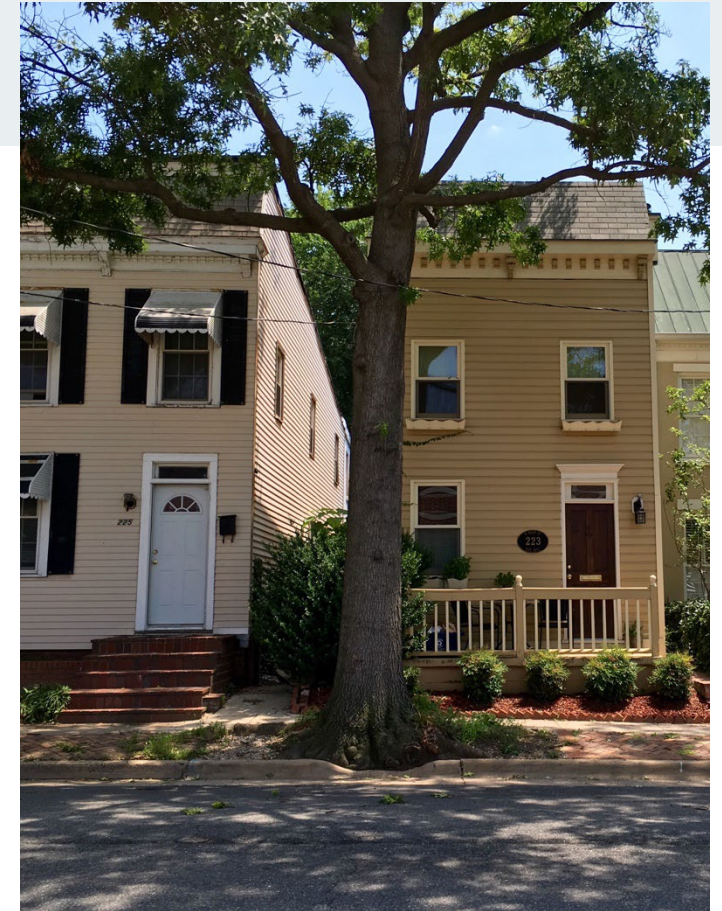
Holding period

- No specific length of time; matter of Exchanger intent

No “dealer/flipper” property “held primarily for sale”

Vacation homes or second homes do not qualify

Changing title/liquidating entity before sale may disrupt qualified use



Personal Use Property

Exchanger's Intent

IRS Safe Harbor Rules For Personal Use of Rental Property

- Replacement Property must be held for at least 2 years
- Exchanger must rent the replacement property for a minimum of 14 days in each of the 2 years; and
- Exchanger's personal use must not exceed 14 days or 10% of the number of days property is rented, whichever is greater.



Fix and Flip Properties



Section 1031 does not apply to flipping

Allows Expenses Payable from Exchange Funds

Examples of Allowable Expenses and Closing Costs:

Real Estate Broker's Commissions

Owner's Title Insurance Premiums

Qualified Intermediary fees

Escrow or Settlement Agent Fees

Recording or Filing Fees

Finder Fees or Referral Fees-
Documentary Transfer Taxes

Attorney & Tax Advisor Fees Related
to the Transaction

Types Of Exchanges

FORWARD EXCHANGE

Sell investment property and, within 180 days, complete the purchase of new investment

REVERSE EXCHANGE

Purchase of new investment property occurs before sale of original investment property (must complete within 180 days)

IMPROVEMENT EXCHANGE

Sell investment property, use accommodator to acquire and hold property while improvements are made.

Can be structured as forward or reverse

Why 1031 Exchanges Are Important?

Like-kind exchanges stimulate business growth

Like-kind exchanges stimulate needed capital investment

Like-kind exchanges help repurpose available real estate

Like-kind exchanges create jobs

Like-kind exchanges help family farmers

Taxes are deferred, not eliminated

Visit www.1031buildsameric.org for more information

NOTE: President Biden's proposed 2024 Budget directly attacks §1031, increases the NIIT and capital gains taxes.

Introduction to: **Advocus National Exchange, LLC**

Karen G. Courtney, *Corporate Counsel – National Commercial Manager, Chicago, Illinois*

Forward 1031 Exchanges Processed by Advocus National Exchange, LLC

- Advocus National Title Insurance Company recently launched its Forward 1031 exchange service offering in partnership with Accruit, one of the nation's leading 1031 Exchange Qualified Intermediaries.
- Through this new service offering, Advocus National 1031 Exchange, LLC—an entity owned and operated by Accruit—serves as Qualified Intermediary.

Forward 1031 Exchanges Processed by Advocus National Exchange, LLC

- Advocus National Title Insurance Company serves as Managed Service Facilitator, and our friendly staff serves as the initial point of contact for forward 1031 exchanges.
- Our staff members work with attorneys and their clients to determine if real estate transactions qualify for treatment as 1031 exchanges and collect the information and documentation required to start the 1031 Exchange process.
- Once qualified for 1031 exchange treatment, our staff uploads the necessary information and documentation to open the 1031 exchange in Exchange Manager ProSM, the patented 1031 Exchange workflow technology provided by Accruit to support this managed service.
- Our staff then connects the attorney and taxpayer with the assigned exchange officer from Advocus National 1031 Exchange, LLC, who will then work with the attorney and taxpayer from that point forward.
- This new service offering reinforces our commitment to empowering real estate investors with tools and expertise to maximize their opportunities.

1031 Exchange Qualifying Questions

1. Qualified Use:

- Is the property held for investment or business?

2. Like-Kind Property:

- Will the taxpayer be reinvesting into property that is like-kind?

3. Same Taxpayer

- Is the same taxpayer selling the property purchasing the replacement property?

1031 Exchange Qualifying Questions

4. Exchange Timeline:

- Is the taxpayer able and willing to complete the sale, and then the purchase within 180 days?

5. Reinvest Equal or Greater:

- Is the taxpayer willing to reinvest equal or greater than the sales price of property they are selling into the purchase property?

6. Related Party:

- Are the seller and buyer related?

Required Exchange Information & Documents

REQUIRED INFORMATION

1. Titleholder Information
2. Taxpayer Name, if different from Titleholder
3. SSN or EIN for Taxpayer
4. Contact Information for all Authorized Signer(s)
5. Relinquished Property(s) Information
6. Closing Date
7. Closing Agent Contact Information

Required Exchange Information & Documents

REQUIRED DOCUMENTS

1. Sales Contract for Relinquished (Sale) Property
2. Title Commitment for Relinquished (Sale) Property
3. If Taxpayer is an entity, the following are required:
 - Single or Multi-member LLC: Operating Agreement
 - Corporation: Corporate Signing Resolution
 - Trust: Trust Documents (Trust Agreement and any Amendments)
 - Partnership: Partnership Agreement

Work with Advocus on 1031 Exchanges

Contact us for more information:

Advocus1031Exchanges@advocustitle.com

Questions?