

Essential 1031 Exchange Strategies

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Why are we here?

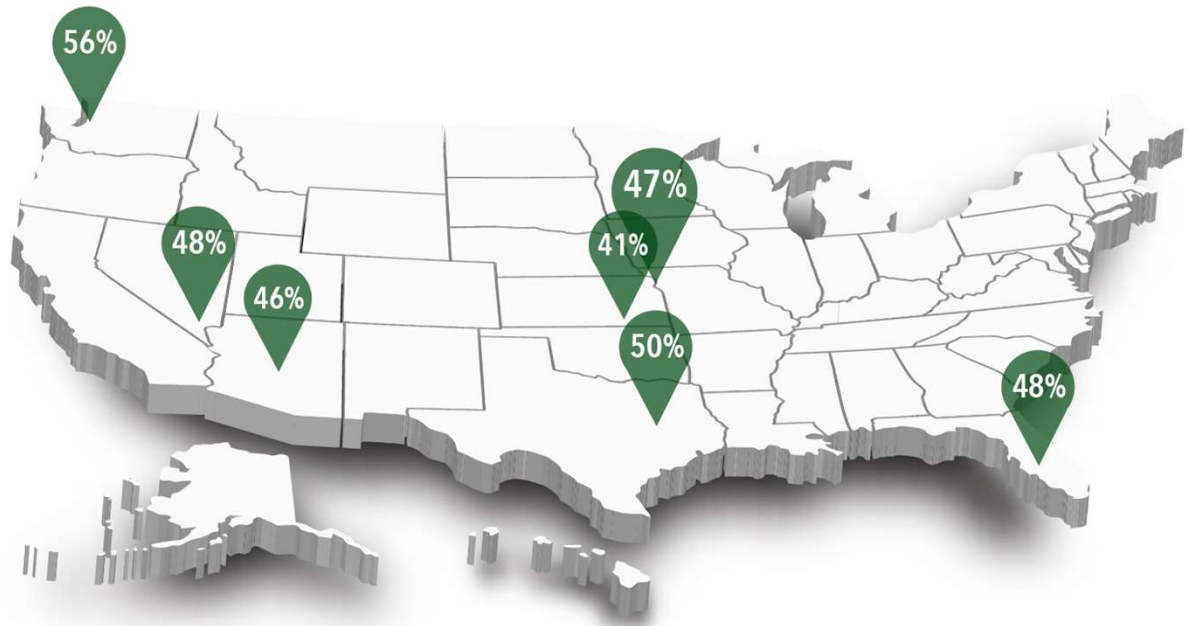
- CE Credit
- Knowledge
- Service
- Preserve Equity for Taxpayers



Statistics

Percentages of Non-Owner Occupied Properties (as of end of 2019)

- Dallas – 50%
- Kansas City – 47.2%
- Las Vegas – 47.5%
- Phoenix – 45.5%
- Seattle – 56.1%
- Tampa Bay – 48%
- Wichita – 40.8%



Overview

- What is a 1031 Exchange?
- What is a Capital Gain?
- How are they taxed?
- Why do a 1031 Exchange?
- How do you choose a Q.I.?
- How does the 1031 work?

PRIOR TO 2018

§1031. Exchange of property held for productive use or investment

(a) Nonrecognition of gain or loss from exchanges solely in kind. —

(1) In general. — No gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.

Internal Revenue
Code

Personal Property

- **Aircraft**
- **Vessels**
- **Livestock**
- **Automobiles**
- **Artwork**



EFFECTIVE JANUARY 1, 2018

§1031. Exchange of property held for productive use or investment

(a) Nonrecognition of gain or loss from exchanges solely in kind. —

(1) In general. — 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 property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.

Internal Revenue
Code

What is Like-Kind?

- Single family house for raw land
- Apartment building for a retail center
- Office building for a warehouse
- 4-plex for a TIC interest in an office building



TAX REFORM

Tax Reform

President Biden's 2023 Budget recommends limiting 1031 Exchanges to \$500,000 gain. Reach out to your Congressional Representative at

www.security1stexchange.com

Security 1st EXCHANGE

Home 1031 Exchange Services Resources News FAQs

There are looming tax changes that could limit the amount of 1031 Exchange deferral to \$500,000. Please support the retention of 1031 Exchanges by sending a message to Congress. [TAKE ACTION](#)

Nationwide Qualified Intermediary Services

Security 1st Exchange offers proven solutions to enhance our client's goals of preserving equity and building their real estate investment portfolios.

[Learn More About Our Services](#)

Have Questions About 1031 Exchanges?

We have the expertise and experience to help guide you through your transaction.

Your Full Name

Email Address

How can we help you?

[Please Contact Me!](#)

TAXES DEFERRED IN A 1031 EXCHANGE

Concept of Capital Gains

$$\begin{array}{r} \text{Sales Price} \\ \text{(Less) } \underline{\text{Cost}} \\ \hline \text{(Equals) Capital Gain} \end{array}$$

Concept of Capital Gains

Sales Price	\$1,000,000
(Less) <u>Cost</u>	<u>(Less) \$ 500,000</u>
(Equals) Capital Gain	(Equals) \$ 500,000

Short Term vs. Long Term Gains

Short Term - 1 year or less

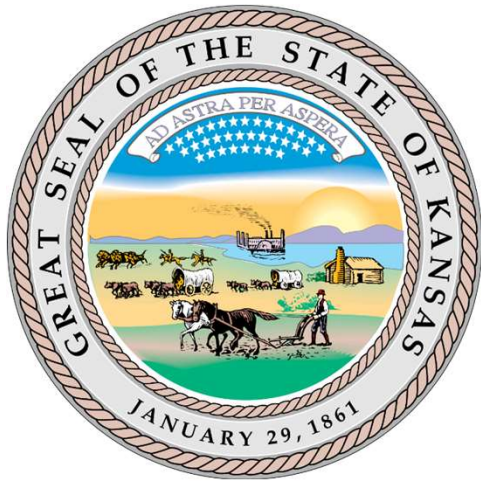
Profit taxed as ordinary income

Long Term - 1 year & 1 day or more

15% Tax Rate for individuals under \$459,750, couples under \$517,200

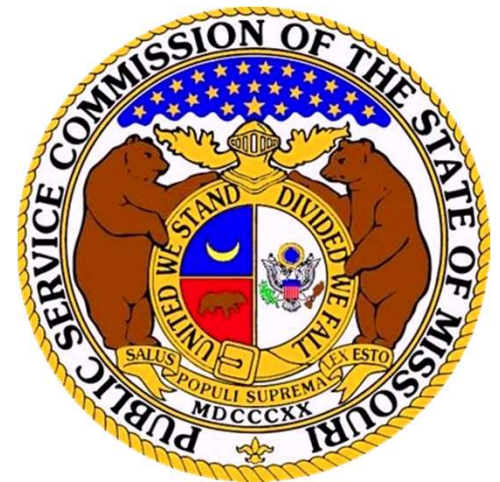
20% Tax rate for taxpayers over the threshold

State Capital Gains



Kansas - 5.7%

Missouri - 6%



Recapture of Depreciation

When an improved property, on which depreciation has been taken, sells for more than its depreciated book value, the depreciation that was taken is taxed at the recapture rate of 25%.



3.8% Net Investment Income Tax

- Began January 1, 2013
- Some people will not have to pay this tax
- Will affect so-called “high-earners”

3.8% Net Investment Income Tax (cont.)

Who are “high-earners”?

- Individuals with an adjusted gross income (AGI) higher than \$200,000
- Married couples with an AGI higher than \$250,000

FINANCIAL REQUIREMENTS

Financial Requirements (cont.)

To defer all taxes, an Exchangor must accomplish two things:

1. Reinvest all proceeds realized from their sale into the replacement property(ies)
2. Reacquire debt equal or greater to the debt paid off from their relinquished property (or replace with fresh cash).

Financial Requirements

Exchanging for equal value and equal equity –

No Boot

Relinquished Prop.

Value: \$1,000,000

Loan: \$ 400,000

Equity: \$ 550,000

Replacement Prop.

Value: \$950,000

Loan: \$400,000

Equity: \$550,000

Financial Requirements (cont.)

Exchanging up in value but equal equity --

No Boot

Relinquished Prop.

Value: \$1,000,000

Loan: \$ 400,000

Equity: \$ 550,000

Replacement Prop.

Value: \$1,200,000

Loan: \$650,000

Equity: \$550,000

Financial Requirements (cont.)

Exchanging for equal value but reduced equity --

Cash Boot

Relinquished Prop.

Value: \$1,000,000

Loan: \$ 400,000

Equity: \$ 550,000

Replacement Prop.

Value: \$1,000,000

Loan: \$600,000

Equity: \$400,000

Financial Requirements (cont.)

Exchanging for reduced value but equal equity --

Mortgage Boot

Relinquished Prop.

Value: \$1,000,000

Loan: \$ 400,000

Equity: \$ 550,000

Replacement Prop.

Value: \$550,000

Loan: \$0

Equity: \$550,000

What is an “Investment Property”?



What is an “Investment Property”? (cont.)

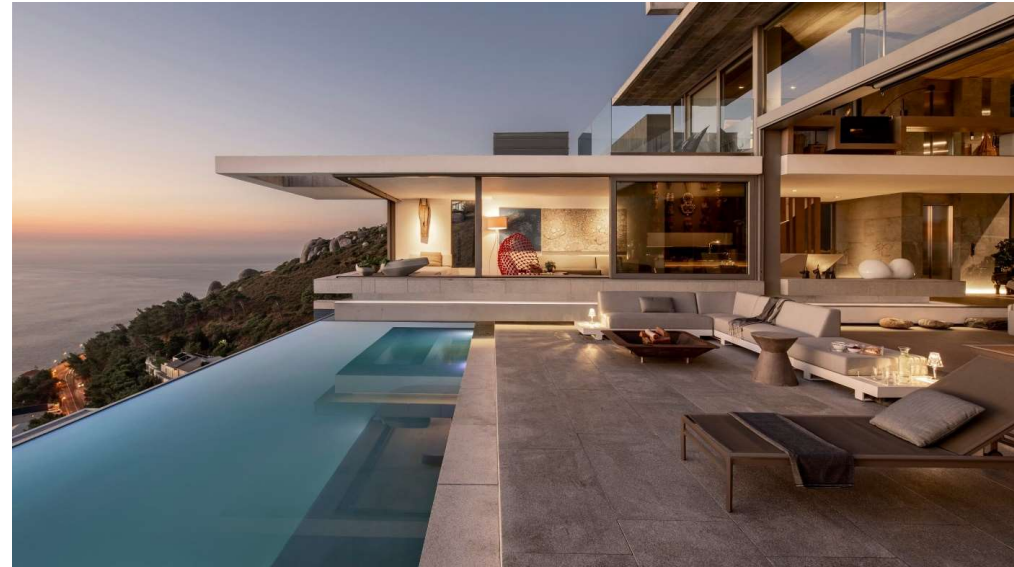
Personal Residence Does Not Qualify



What is an “Investment Property”? (cont.)

Revenue Procedure 2008-16

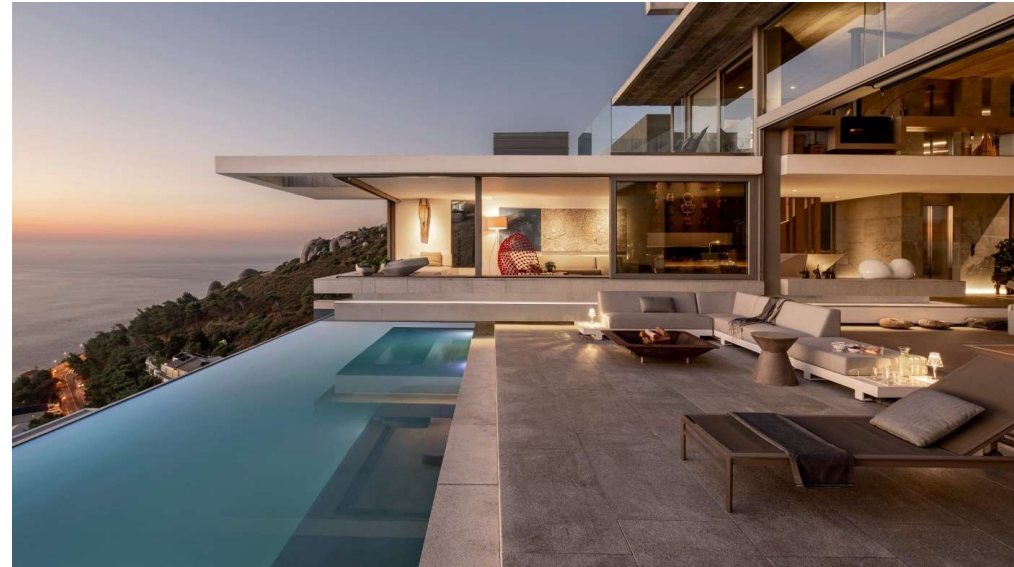
Safe Harbor for Exchanges of
Vacation Homes and Conversions
to or from Personal Residences



What is an “Investment Property”? (cont.)

The vacation home qualifies if:

- Effective for exchanges after March 10, 2008
- Own the home for at least 24 months
- Rent it for at least 14 days for each 12-month period
- Personal use of no more than the greater of 14 days per year or 10 percent of rental time of the property.



What is an “Investment Property”? (cont.)

Stock in Trade Does Not Qualify



What is an “Investment Property”? (cont.)

Stocks, Bonds & Notes DO NOT Qualify



What is an “Investment Property”? (cont.)

Interest in a Partnership DOES NOT Qualify

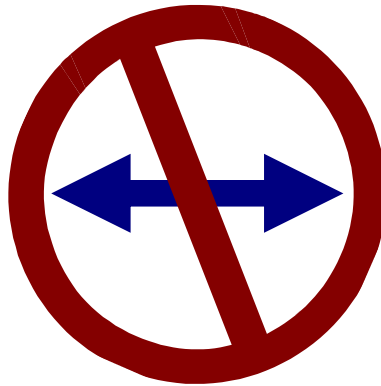


What is Like-Kind?

- Single family house for raw land
- Apartment building for a retail center
- Office building for a warehouse
- 4-plex for a TIC interest in an office building



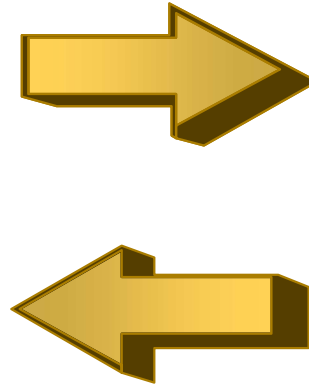
Property MUST be in the U.S.



PLR 9038030 – Virgin Islands (1998)

Section 1.935-1T – Guam & Northern Mariana Islands (2005)

Multiple Properties Qualify



TIMEFRAMES

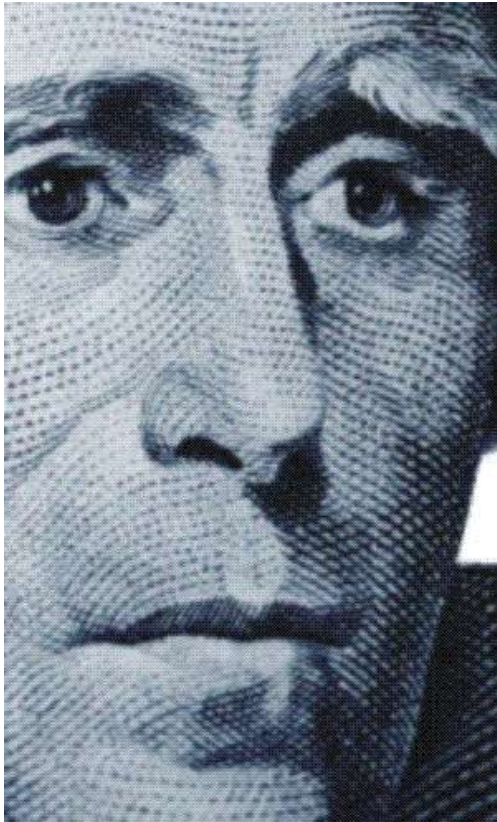
Timeframes for an Exchange



45 day Identification Period

180 day Exchange Period

Timeframes for an Exchange (cont.)



§1031 adopted in 1921

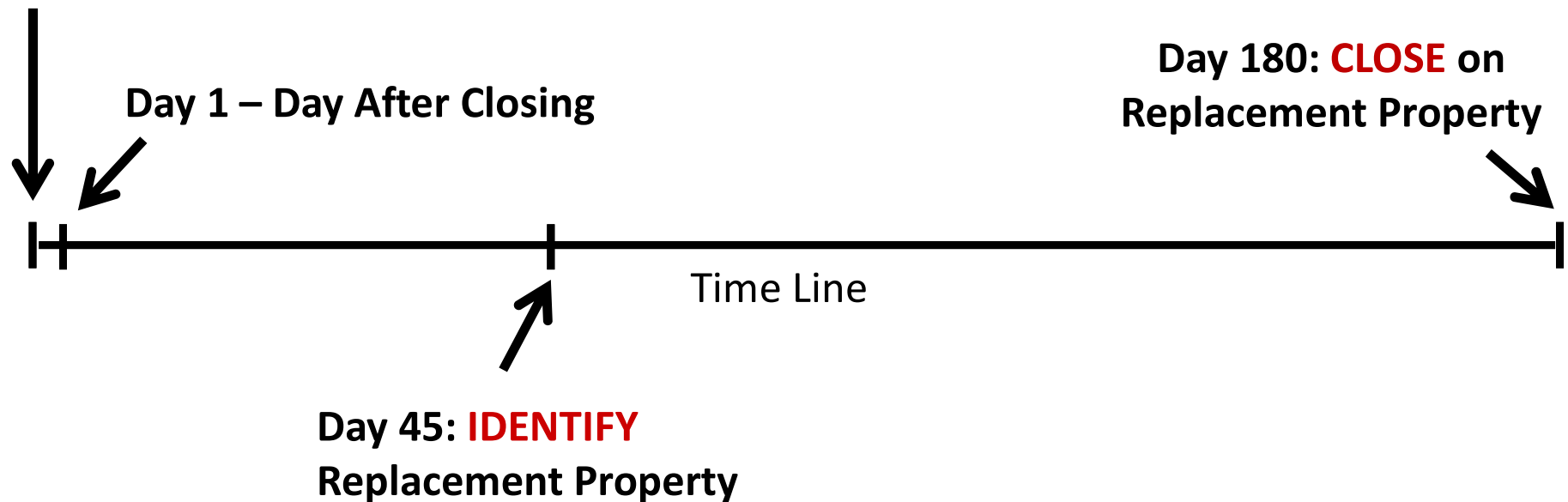
First Exchange – 1967

Approved – 1979

Deficit Reduction Act - 1984

Timeframes for an Exchange (cont.)

Day 0 – Closing of Relinquished Property



THE QUALIFIED INTERMEDIARY

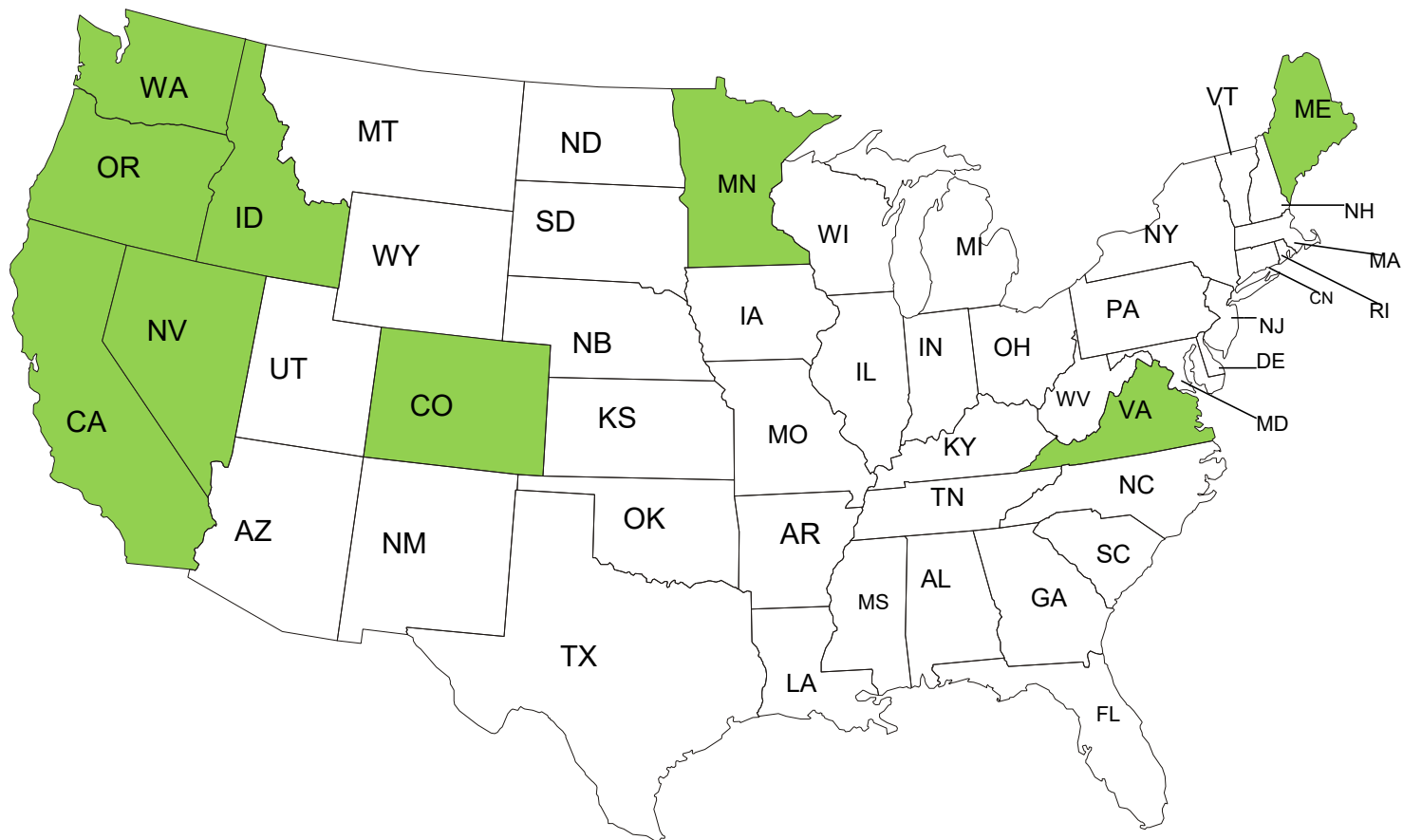
How do you choose a QI?

Security

Knowledge and Experience

“Qualified” per regulations

States with QI Laws



How do you choose a QI?

“Qualified” per regulations

If you are doing an exchange in Washington, Oregon, California, Nevada, Idaho, Colorado, Minnesota, Virginia or Maine, is your QI in compliance with those states' specific regulations?

THE DELAYED EXCHANGE STEP BY STEP

Delayed Exchange - Steps



1. Taxpayer retains services of independent tax advisor.
2. Taxpayer enters into agreement to sell property, including recital that Taxpayer intends to relinquished property as part of a 1031 Tax Deferred Exchange.

Delayed Exchange – Steps (cont.)



3. Open escrow / open 1031 Exchange
4. Taxpayer enters into Exchange Agreement with Q.I. which becomes a principal in each transaction, not an agent
5. The first half of the exchange closes with the transfer of the Relinquished Property

Delayed Exchange – Steps (cont.)



6. Taxpayer identifies Replacement Property(ies) on or before the 45th day after the transfer of the Relinquished Property. The Identification Letter is sent to the Q.I.

Delayed Exchange – Steps (cont.)

Identification Rules

- **3 Property Rule** – up to 3 properties no matter what their value
- **200% Rule** – any number of properties having aggregate value not more than 200% of Relinquished Property
- **95% Exception** – any number of properties at any values provided that taxpayer acquires 95% of the identified properties.

Identification Form



Security 1st EXCHANGE

REPLACEMENT PROPERTY IDENTIFICATION FORM - 3 PROPERTY RULE

Exchange No.:	Deadline:	Exchanger:	Relinq. Property Address:	Relinq. Prop. Sale Price:	Exchange Funds:
Test		John Doe	100 Main Street	\$500,000.00	\$500,000.00

This form is required to be completed and returned to Security 1st Exchange no later than the deadline date shown above.

Please review the following requirements and contact our office if you have any questions.

- Replacement Property must be unambiguously described by means of a street address, legal description, and/or distinguishable name.
- No changes can be made to this form after the expiration of the 45-day identification period.
- If you will not be acquiring 100% of the ownership interest, please enter the approximate ownership interest to be acquired.

This form must be completed and sent to Security 1st Exchange LLC, on or before the deadline specified above.

Note – If you wish to identify more than three properties, please contact us for further instructions.

The undersigned hereby identifies the identified properties as replacement property for the above referenced tax-deferred exchange as required by Internal Revenue Code § 1031(a)(3)(A) and Treas. Reg. § 1.1031(k)-1(c).

Property 1: _____ **Ownership:** _____ %

(Street Address) (City) (State) (Zip)

(Legal Description)

Property 2: _____ **Ownership:** _____ %

(Street Address) (City) (State) (Zip)

(Legal Description)

Property 3: _____ **Ownership:** _____ %

(Street Address) (City) (State) (Zip)

(Legal Description)

This identifies the properties I have or will be able to acquire within the 180-day exchange period. I understand that after the 45-day identification period, the exchange funds may only be used to acquire properly identified properties. Any remaining funds will be available for release to me only after 1) All of the properties on this form have been acquired (or if specifically indicated, the number of properties specified or 2) the expiration of the 180 day exchange period.

John Doe

Date

Delayed Exchange – Steps (cont.)

Identification of Replacement Property



Description of property must be unambiguous

Delayed Exchange – Steps (cont.)

Identification of Replacement Property

- Delivered or sent before midnight on the 45th day
- Identify all replacement properties
- On a written document
- Signed by the Taxpayer

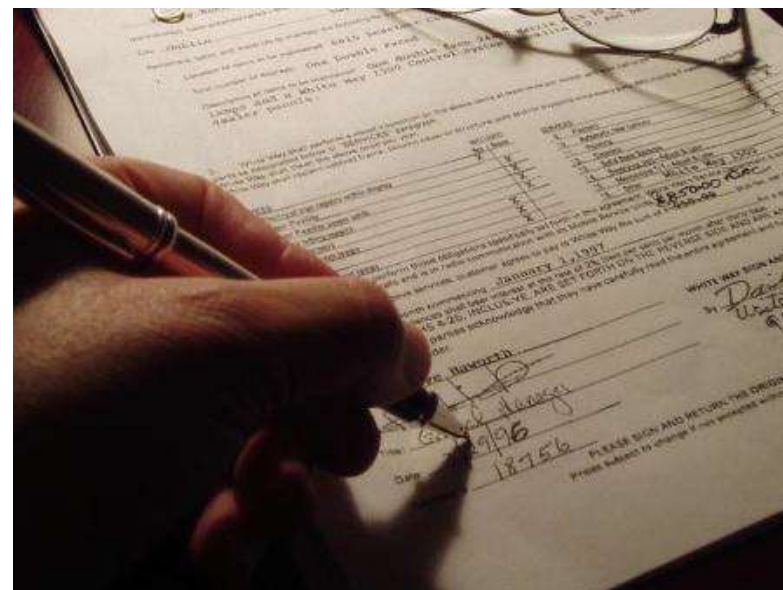
Delayed Exchange – Steps (cont.)

Revocation or Amending of Identification

- Delivered or sent before midnight on the 45th day
- Identify all replacement properties
- On a written document
- Signed by the Taxpayer

Delayed Exchange – Steps (cont.)

7. Taxpayer enters into agreement to acquire Replacement Property, including recital that Taxpayer intends to acquire property as a part of a 1031 Exchange (of equal or greater value than Relinquished Property).



Delayed Exchange – Steps (cont.)

8. Open escrow / call 1031 Exchange
9. Exchange closes with the acquisition of the Replacement Property – or in stages if multiple properties are involved – all within 180 days of the transfer of the relinquished property.



TITLE PARKING EXCHANGES

Reverse Exchange

"I want to purchase a property before I will be able to sell the property I currently own."



Reverse Exchange (cont.)

- Safe Harbor possible (since 9/15/00)
- Exchangor finances replacement property purchase
- EAT holds title and waits sale of relinquished property
- Sale repays purchase note



Improvement Exchange

- QI holds title and makes approved improvements
- Investment replaced before 180 days
- Title transferred to Exchangor



SUMMARY

An agent's reaction to a 1031 Exchange

If a client sells a property through an exchange, he must...



BUY A NEW PROPERTY!



If your client is selling a property and doing a 1031 Exchange, you could get at least 2 deals out of it.
If they buy multiple properties, you could get more!

Key things to remember

- Purchase like kind property
- 45 day Identification Period
- 180 day Exchange Period
- Purchase of equal or greater value by
 - Spending all of the cash (equity)
 - Reacquiring debt equal or greater
- Do your research when selecting a Qualified Intermediary

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