UNDERSTANDING
1031 Exchanges

A 1031 Exchange, also known as a Like Kind Exchange, is a way of structuring a sale of certain kinds of property so that the seller's profit or gain is not currently taxed. Instead, the property that is sold is replaced with another "like kind" property.

Like Kind Property

The replacement property title must be taken in the same name as the relinquished property was titled.

If a husband and wife own property in joint tenancy or as tenants in common the Replacement Property must be deeded to both spouses, either as joint tenants or as tenants in common. Corporations, partnerships, limited liability companies, and trusts must be in title on the Replacement Property the same as they were on the Relinquished Property.

- Improved real estate can be replaced with unimproved real estate.
- Unimproved real estate can be replaced with improved real estate.
- A 100% interest can be exchanged for an undivided percentage interest with multiple owners and vice versa.
- One property can be exchanged for two or more properties. Two or more properties can be exchanged for one Replacement Property.
- A duplex can be exchanged for a four-plex. Investment property can be exchanged for business property and vice versa.

Real Estate Interests Which Qualify as Like-Kind for a 1031 Exchange

- Fee interest
- Fractional (tenancy-in-common) interest
- Leasehold interest, 30-year plus lease
- Easements for conservation
- Easements for right of way
- Water Rights
- Mineral Rights
- Oil & Gas interests
- Transferable Development Rights
- Mutual Irrigation Ditch Stock

Timing

The exchange must be completed 180 days from the recorded date of relinquished property title deed.

Identification of replacement property must be completed within the first 45-days of the recorded date of relinquished property title deed.

1031 Exchange Types

Simultaneous Exchange

The closing of the relinquished property and the replacement property occur on the same day, usually back-to-back. There is no interval of time between the two closings. This type of exchange is covered by safe harbor regulations.

Delayed or "Starker" Exchange

The replacement property is closed at a later date than the closing of the relinquished property. This type of exchange is sometimes referred to as a "Starker Exchange" after the well-known Supreme Court case which ruled in the taxpayer's favor for a delayed exchange before the Internal Revenue Code provided for such exchanges. There are strict timeframes established by the Code and Regulations for completion of a delayed exchange, namely the 45-Day Clock and the 180-Day Clock.

Reverse Exchange (Title-Holding Exchange)

The replacement property is purchased and closed on before the relinquished property is sold. Usually, the Intermediary takes title to the replacement property and holds title until the taxpayer can find a buyer for his relinquished property and close on the sale under an Exchange Agreement with the Intermediary. This occurs subsequent or simultaneous to the closing of the relinquished property, the Intermediary conveys title to the replacement property to the taxpayer.

1031 Exchange Types (cont.)

Improvement Exchange (Title-Holding Exchange)

A taxpayer desires to acquire a property and arrange for construction of improvements on the property before it is received as replacement property. The improvements are usually a building on an unimproved lot, but also include enhancements made to an already improved property in order to create adequate value to close on the Exchange with no boot occurring. The Code and Regulations do not permit a taxpayer to construct improvements on a property as part of a 1031 Exchange after they have taken title to the property as replacement property in an exchange. Therefore, it is necessary for the Intermediary to close on, take title and hold title to the property until the improvements are constructed and then convey title to the improved property to the taxpayer as replacement property. Improvement Exchanges are done in the context of both Delayed Exchanges and Reverse Exchanges, depending on the circumstances.

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