A Little Less Taxing…

1031 Exchanges Made Easy by

1031 Tax Free Strategies, LLC
12853 Banyan Creek Drive
Fort Myers, FL 33908

239-333-1031
239-466-5496 Fax

www.1031company.com
Email information@1031company.com

Please note – this information is presented to help you make an informed decision in completing a 1031 Exchange. It is not a substitute for a qualified tax advisor. Please consult your tax advisor regarding your situation.

A Little Less Taxing…

How to get started on exchange?

Please remember that all paperwork for your 1031 Exchange must be completed before you sell your relinquished or your replacement property. You must use a qualified intermediary to complete a 1031 Exchange.

List below is the information needed complete 1031 Exchange. Once you have completed the form below, please fax to our office at 239-466-5496.

1031 Info Sheet Date: _____________

Seller/Exchangor: ____

Address: ____

City: ____

State: ____

Zip: ____

E-mail: ____

Telephone/Cell/Office: ____

Fax: ____

Date of Closing on Relinquished Property: ________________________

Selling Price of Property: _______________________________________

Title/Closing Agent and Phone: ___________________________________

Address of Property Sold: ____

Seller's Federal ID Number(SSN): _________________________________

Realtor: ____

Replacement Property Sellers: ____

Replacement Property Address: ____

Replacement Property City, State, and Zip: ______________________________________

Closing Date on Replacement Property: ____

Closing Agent on Replacement Property: ____

Please note – this information is presented to help you make an informed decision in completing a 1031 Exchange. It is not a substitute for a qualified tax advisor. Please consult your tax advisor regarding your situation.

Now to the nitty gritty – 1031 Exchanges can be easy if you follow the rules laid out by the IRS. Don't be overwhelmed by the terminology or number of rules, they are not that bad. To complete your exchange you must use a Qualified Intermediary. Please feel free to call us a 239-333-1031, if you have more questions.

What is a 1031 exchange?

Internal revenue code section 1031 provides that no gain or loss will be recognized on the exchange of any type of business use or investment property for any other business use or investment property. 1031 exchanges are not really exchanges in the context of two-party barter. Instead, they are typical sales and purchases that involve the same exact ingredients as any other sale or purchase, without the capital gains. The only real difference is the investor is increasing his selling and buying power by electing to avoid the drain of taxes under section 1031 regulations. No other aspects of the transaction are affected.

Who should consider a 1031 exchange?

Anyone who is thinking about selling a business use or investment property should consider affecting a 1031 exchange. An exchange offers the astute investor an opportunity to reinvest the federal capital gains that would normally be handed over to the irs and put that money to work for himself. You work too hard to simply pay the tax without carefully considering this reinvestment option. Essentially, 1031 exchanges should be thought of as an interest free loan from the irs; one in which the principal may be increased through subsequent exchanges and may never require repayment, if you plan properly.

Misconceptions about exchanging

1. Many still believe that you must "swap" properties. Although this was required in the original code, this is rarely done in present times. 1031 exchanges now enable one to sell their property to someone totally unrelated to the person from whom they are purchasing their replacement
2. Many believe only investors of large commercial properties can utilize the benefits of section 1031. The great thing about 1031 exchanges is that it applies to all investment properties, large and small. It will work the same way for a corporation selling a large shopping center as it would for an individual selling a single-family home used as a rental property in a vacation area.
3. Many believe you must acquire a property of "similar use or service." While 1031 exchanges are also known as "like-kind" exchanges, like-kind simply applies to real property held for business use or investment. Therefore, an investor may sell raw land and

acquire a five-unit apartment building or sell a warehouse and acquire raw land. He can sell one property and acquire three or sell four and acquire one. Virtually any type of real property used for business use or investment will qualify.
4. Many believe 1031 exchanges are very complicated and not worth doing. The fact is that when working with a qualified intermediary who specializes in Section 1031 tax deferred exchanges, the exchange process is very simple. The intermediary will keep you aware of your time deadlines and ensure you do everything in strict compliance with IRS regulations.

ADVANTAGES OF EXCHANGING
1. The Exchanger will have more buying power because the federal income taxes are deferred. This will enable him to leverage himself up greater than he could have he paid the tax liability. The additional equity to reinvest will make him a more solid buyer and help him get easier financing.
2. Investors can do exchange after exchange to create a pyramiding effect. This tax liability is forgiven upon the death of the investor as the heirs get a stepped up basis on the inherited property.
3. The Exchanger will have greater selling power because he does not have to inflate the sales price to try to cover some of the capital gains that would normally be due upon the sale of an investment property. It will enable him to be more flexible with the selling price.
4. The Exchanger can acquire a replacement property with greater income potential. He can sell raw land and acquire income-producing property. Perhaps, he wants to acquire a building with additional units or in an easier to rent location.
5. The Exchanger has the opportunity to consolidate several hard to manage properties in one easy to manage property or diversify several small properties into one large property. It provides an excellent opportunity to relocate or expand a current business or investment.
6. An exchange can also help an investor acquire a less management intense property.

BESIDES TAX REDUCTION,
1031 EXCHANGES CAN ACCOMPLISH MANY INVESTMENT GOALS:

- Estate preservation
- Increased buying power because of greater cash flow
- Increased selling power because the federal capital gain tax liability is deferred
- Exchange for property with an increased income (more rental units, higher rental income per unit, lower operating expenses, easier to rent location, etc.)
- The need or desire to relocate a business or investment property
- Exchange for property that requires less management
- Exchange for property that is easier to finance
- Consolidate smaller properties into a larger property

- Diversify a large property into several smaller properties
- The need or desire to expand a business into a larger space

All of the above culminates into one significant power-
The ability to create pyramiding wealth accumulation in real estate ownership.

SLIGHT DISADVANTAGE
The basis of your replacement property will be lowered by the amount of gain deferred on the sale of your relinquished property. However, when weighing this against the deferred gain, the astute investor can clearly see he is still significantly ahead.

THE PROPERTIES IN THE EXCHANGE

RELINQUISHED PROPERTY:
The relinquished property is the business use or investment property the Exchanger owns and wants to sell via the 1031 Exchange.

REPLACEMENT PROPERTY:
The replacement property is the business use or investment property the Exchanger wants to acquire to complete the 1031 Exchange.

There can be more than one of each of the relinquished and replacement properties. For example, an Exchanger can sell three small properties and purchase one large property or sell one large property and acquire four smaller ones. An Exchanger does not have to purchase the same type of property. For example, he can sell a storage facility and acquire an apartment building or sell a raw piece of land and acquire a shopping center.

THE PARTIES INVOLVED IN THE EXCHANGE

EXCHANGER:
The Exchanger is the taxpayer who is electing to defer the capital gains by affecting a 1031 Exchange.

SELLER:
The seller is the person who owns the property the Exchanger wishes to acquire as a replacement property.

BUYER:
The buyer is the person who wants to purchase the property the Exchanger is selling

INTERMEDIARY:
The use of a qualified Intermediary is required by the regulations of Section 1031. The role of the Intermediary is to act as a middleman in both the sale and purchase transactions

BASIC REQUIREMENTS OF EXCHANGES

1. BOTH PROPERTIES MUST BE "LIKE-KIND".

- Like-kind simply means real property.
- Like-kind refers to the nature or character, not its grade or quality.
- Like-kind is a very broad and liberal category where just about any type of investment or business use property would qualify.
- Properties can be located anywhere within the United States with Exchanges taking place in one or more states.
- Examples of like-kind: rental properties (single family homes, duplexes, triplexes, apartment buildings and complexes, etc.), raw land, office buildings, shopping centers businesses, marinas, golf courses, a lease of at least 30 years including options, parking lots, farms, factories, trailer parks, storage facilities, retail stores, interest in a co-tenancy.
- Examples of non like-kind: stocks, bonds, notes, interest in a partnership, personal property, certificates of trust, chooses in action.
- Investors can "mix and match" their properties. For example, an investor can sell a duplex and acquire raw land or sell a parking garage and acquire a multi-unit apartment building and a warehouse.

2. BOTH PROPERTIES MUST BE HELD FOR INVESTMENT OR BUSINESS USE.

- Your use of both the relinquished property and replacement property must be investment or business use; each for a minimum of one to two years.
- Properties must not be used for personal use for more than 14 days per year or 10% of the actual number of days the property has been rented in a given year.
- Replacement property cannot be purchased with the intent to sell immediately.

3. EXCHANGER MUST USE A QUALIFIED INTERMEDIARY OR FACILITATOR.

- One of the safe harbors of the regulations is the use of a qualified Intermediary to facilitate the Exchange.
- The sale of the relinquished property and the acquisition of the replacement property must "flow" through the Intermediary. This is done through direct deeding to avoid duplicate transfer taxes.
- The qualified Intermediary may not be the taxpayer or an agent of the taxpayer (realtor, attorney, tax advisor, banker, accountant, employee, etc.) or lineal descendant of the Exchanger.

4. Exchanger must use a qualified escrow agent and have no actual or constructive rights to the sale proceeds of the relinquished property.

- The qualified escrow agent may not be the taxpayer or an agent of the taxpayer (realtor, attorney, tax advisor, banker, accountant, employee, etc.) Or lineal descendant of the exchanger.
- The exchanger must not have access to the sale proceeds of the relinquished property.
- The exchanger is entitled to all earnings on the escrow funds. These taxable funds must also be restricted in the same manner as the principle.
- The exchanger chooses the escrow agent.
- The exchanger is entitled to obtain security for his funds.

5. The proper documentation must be used in order to comply with 1031 regulations.

- 1031 exchange agreement between the exchanger and the intermediary
- This is the most important document in the exchange. It is the document in which the exchanger gives the intermediary the right to acquire the relinquished property from the exchanger and convey it to the buyer. It also gives the intermediary the right to acquire the replacement property from the seller and then convey it to the exchanger.
- 1031 exchange escrow agreement between the intermediary and escrow agent
- If island financial is acting as both your intermediary and escrow agent, the escrow agreement will be incorporated into the 1031 exchange agreement between the exchanger and the intermediary.
- 1031 exchange amendment and assignment for the rollover of the relinquished property
- Assigns the exchanger¹s rights in the agreement of sale with the buyer to the intermediary.
- Serves as written notification to the buyer of the relinquished property of exchanger¹s intent to effect a 1031 exchange and also provides a hold harmless clause to assure the buyer that there are no additional liabilities or costs to him.
- If a 1031 exchange clause is inserted into the agreement of sale, this document is unnecessary.
- 1031 exchange amendment and assignment for the acquisition of the identified replacement property
- Assigns the exchanger's rights in the agreement of sale with the seller to the intermediary.
- Serves as written notification to the seller of the replacement property of the Exchanger¹s intent to effect a 1031 Exchange and also provides a hold harmless clause to assure the seller that there are no additional liabilities or cost to him.

- If a 1031 Exchange Clause is inserted into the Agreement of Sale, this document is unnecessary.

6. Exchanger must adhere to time limitations.

- The 45-day identification period begins at the closing of the relinquished property and requires the identification of like-kind replacement property.
- During this 45-day identification period, you may revoke an identification and make a new one.
  * if a like-kind replacement property has not been properly identified to the intermediary by midnight of the 45th day, the exchange will not work and the taxpayer will be unable to defer the capital gains.
- The 180-day exchange period runs concurrently with the 45-day identification period and requires the acquisition of at least one of the identified replacement properties.
  * if the settlement of the relinquished property occurs between october 16 and december 31 of the current year, the 180-day exchange period will be shortened to the income tax deadline of april 15 of the next calendar year unless a timely and proper irs extension is filed for their return. For a corporation, this filing date is march 15 of the next calendar year unless an irs extension is filed.

Limitations on the number of replacement properties that can be identified:

1. Three property rule:
exchanger may identify up to three properties regardless of their fair market value. The exchanger is not obligated to purchase all three properties but must purchase at least one of the three identified properties. For example, if selling a relinquished property for $100,000, three replacement properties can be identified with a combined fair market of $ 750,000.
2. 200% value rule:
exchanger may identify more than three properties but their combined or fair market value cannot exceed double (200%) the fair market value of the relinquished property. For example, if a relinquished property was sold for $100,000 and four or more replacements are identified, their combined fair market value cannot exceed $200,000 with 200% or double the sale price of the relinquished property.

Exceptions to the Three Property Rule and the 200% Value Rule:

1. Any replacement property acquired within the 45-day Identification Period will be treated as properly identified, regardless of whether or not it is within the Three Property Rule or 200% Value Rule.

2. If the Three Property Rule and 200% Value Rule are violated, the property will still be treated as properly identified, provided that 95% of the combined fair market value of the identified replacement property has been acquired. For example, assume a $100,000 property was sold and five properties with a combined fair market value of $800,000 are identified. This will be treated as properly identified provided all five properties are acquired. It is almost impossible to acquire 95% of the property without acquiring all 100% of the property.

Frequently Asked Questions

Where the Escrow Money is Kept During the Exchange - Your money will be kept in a separate escrow account during the exchange process. We are also bonded to insure your comfort during exchange process.

Your money will earn interest while it is held in our exchange account. Interest is competitive at market rates. Any interest earned will be taxable to the Exchanger.

What are the Fees for Exchanges (as of July 1, 2005) subject to change -

Simultaneous or Delayed Exchange - The fee table for a standard exchange is as follows:

Sale Price	Fee
under $100k	$ 600
$100k - $250k	$ 750
$250k - $500k	$ 950
$500k - $1M	$1,250
over $1M	$1,500

This will include preparation of all documents, communication with your closing agent and consultation to answer any of your questions. It is an all-inclusive fee which includes handling of both the relinquished and the replacement property.

This is the fee for the exchange of one property. If you are acquiring more than one property, the additional fee is $150.00 per property. This will include preparation of all documents, communication with your closing agent and consultation to answer any of your questions. Your money will receive interest while it is in the possession of our company.

Reverse Exchanges - Reverse exchanges are all unique. A typical fee for a reverse exchange is $3,300. Please call for more information.

For other exchanges including construction exchanges or reverse exchanges, please call 239-333-1031 for more information.

What is a Reverse Exchange - Buying your Replacement Property First

Because of favorable tax law changes, Reverse Exchanges have become commonplace over the last few years; they can provide great opportunities and advantages in managing your real or personal property investments.

As the name suggests, the Reverse Exchange works through the "exchange"of property. Upon the sale of an investment property, you can defer all capital gains tax by purchasing a replacement property. A Reverse Exchange is different from a 1031 Exchange, mostly because it allows you to purchase property first, then sell your existing investment. Reverse Exchanges are typically used in the following situations:

• The owner of investment property listed for sale finds the ideal replacement property before finding a buyer for the exchange property.
• After substantial real estate appreciation, the common complaint is lack of inventory; therefore, the real estate investor needs to purchase prime real estate as it enters the market.
• Real estate sellers are confident in being able to sell their exchange property, but wish to avoid having to identify the replacement property in the 45 days required by a 1031 Exchange. Therefore, they purchase model replacement property now.

The most common question asked regarding an Exchange is: "May I buy a property first, then sell my current property?" The answer is yes because of a new IRS law. Effective September 15, 2000, the IRS issued its Revenue Procedure 2000-37.With this law, for the first time, the IRS sanctioned the Reverse Exchange with the "safe harbor" rule. Essentially, the IRS has approved a parking arrangement. If a real estate seller cannot sell their property in a timely enough fashion to perform a standard 1031 Exchange, they can now use a Qualified Intermediary to hold title on the property they wish to acquire. The highlights of the Revenue Procedure are as follows:

• Reverse Exchanges must be completed in 180 days. The 180 days starts from date the Intermediary purchases the replacement property for the taxpayer.

• Within 45 days of the purchased parked property, an identification form must be completed that identifies the relinquished property that is to be sold.

• A new document called a "Qualified Exchange Accommodation Agreement" must be completed by the Qualified Intermediary and the taxpayer.

Can I do an Exchange between related party and/or Relative? -

An exchange between related parties gets close scrutiny from the IRS.

The IRS was concerned that related parties would engage in abusive basis shifting, as outlined in the legislative history:

To curb these abuses, the IRS established a mandatory two year holding period for exchanges between related parties.

If the exchange is between related parties, the transaction will not qualify for non-recognition treatment if either party disposes of property received in the exchange during the two year holding period.

The two year period commences on the date of the last transfer required to complete the exchange.

Gain must be recognized on each of the original transfers, as of the date of disposition of the property.

You cannot buy replacement property from a related party unless the related party is performing a 1031 exchange.

Number one 1031 Question - How much do I need to spend to defer all the taxes in a 1031 Exchange?

This is the number one 1031 question. If you want to defer all the tax on the sale of your relinquished property, you must purchase a property equal or great than net selling price of your relinquished property. What is net selling price – Net selling price is Gross sales prices less closing costs. Typically closing costs include real estate commissions, title fees and transfer costs.

Example

Sales Price	$200,000
Closing Costs	15,000

Net Selling Price	$185,000

If the taxpayer purchases replacement property in excess of $185,000 they should defer all the tax on the transaction. If they purchase less then $185,000 they will pay capital gains tax on the difference.