JLM Corporation

"Your source for Section 1031 Deferred Exchanges since 1988"

A subsidiary of Orange Coast Title Company

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- **What is an Exchange** – Section 1031 of the Internal Revenue Code allows a party in a qualified transaction to sell real property held for business , trade, or investment purposes and to defer capital gains by purchasing "like kind" exchange property within the applicable timeframes
- **Who Should Exchange –** A taxpayer who has real property that may net them a gain upon the sale (generally property that has been substantially depreciated for tax purposes and/or has appreciated in fair market value).
- **Why Exchange** – Defer paying capital gain taxes, relief from property management, to diversify, if you own multiple properties, if you relocate, if you would like to change property types.
- **Exchange Rules** – The real property bought and sold must be held for productive use in a trade or business, or for investment purposes, and must be like kind. The sale proceeds must be transferred directly from escrow to the Qualified Intermediary (QI). The exchanger cannot have constructive or actual receipt of the sale proceeds. The sale proceeds must be invested in a real property also to be held for business , trade,or investment purpose. Any cash retained by the taxpayer will be subject to taxation. The replacement property must be of equal or greater value than the property sold. The replacement property must be subject to an equal level or greater level of debt than the relinquished property, or the buyer will either have to pay taxes on the amount of the decrease, or have to put in additional cash funds to offset the lower level of debt in the replacement property. The replacement property must be identified and escrow closed within the applicable timeframe.
- **Exchange Timelines** – Identify replacement property within 45 days of closing on sale of relinquished property.

  Close on purchase (replacement) property must occur on the earlier of 180 days from sale of relinquished property, or the date on which tax returns are due for the calendar year in which the relinquished property is sold (April 15th)
- **Like-kind Property** – Exchange any real property for any other real property in the United States. Properties must be held for productive use in business, trade or investment e.g., allows exchange of apartments for vacant land, etc.
- **Identification of Replacement Property** – **3 property rule**: Exchanger may identify 3 properties without regard to market value. **200% rule**: Identify any number of replacement properties as long as the aggregate value of those properties does not exceed 200% of the value of the relinquished property (Need evidence of value). **95% rule**: Any number of properties may be identified as long as the exchanger purchases at least 95% of the aggregate value of all properties identified.
- **Title Holding Rules –** The party who sells must be the party who buys. Watch out for corporations, LLCs, Trusts, etc. (There are some exceptions, such as individuals and single-member LLCs).
- **Reverse Exchange –** Exchanger purchases replacement property first, then sells the relinquished property. Title of the replacement property passes to an Exchange Accommodation Title Holder ("EAT").
- **Failure to Close Exchange –** Exchanger may pay capital gains taxes. State withholding taxes will be withheld by QI pursuant to California law.
- **Avoid Common Mistakes –** Personal residences do not qualify; find a reliable QI; watch your timing – you must inform escrow and the buyer/seller and have your client identify an intermediary; **count your days** – make sure your client identifies timely and escrow closes within the applicable time period; straighten out vesting issues prior to escrow. Understand your client's investment objectives and the goals of all parties.