



1031 Property Exchange Basics

Exchanges protect investors from capital gain taxes as well as facilitating significant portfolio growth and increased return on investment. In order to access the full potential of these benefits, it is crucial to have a comprehensive knowledge of the exchange process and the IRC. It is important to obtain the services of a Qualified Intermediary as defined and required by the IRC and Treasury Regulations

A properly structured exchange allows an investor to sell a property, and reinvest the proceeds in a new property deferring all capital gain taxes.

IRC §1031 (a)(1) states: *"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."*

To understand the powerful protection an exchange offers, consider the following example:

- An investor has a \$200,000 capital gain and incurs a tax liability of approximately \$70,000 in combined taxes (depreciation recapture, federal and state capital gain taxes) when the property is sold. Only \$130,000 remains to reinvest in another property.
- Assuming a 25% down payment and a 75% loan-to-value ratio, the seller would only be able to purchase a \$520,000 new property.
- If the same investor chose to exchange, however, he or she would be able to reinvest the entire \$200,000 of equity in the purchase of \$800,000 in real estate, assuming the same down payment and loan-to-value ratios.

As the above example demonstrates, exchanges protect investors from capital gain taxes as well as facilitating significant portfolio growth and increased return on investment. In order to access the full potential of these benefits, it is crucial to have a comprehensive knowledge of the exchange process and the IRC. For instance, an accurate understanding of the key term "like-kind" - often mistakenly thought to mean the same exact types of property - can reveal possibilities that might have been dismissed or overlooked. API is your resource to obtain accurate and thorough information about the entire exchange process.

A properly structured exchange is the transfer of property for property, thus deferring capital gain taxes. Any cash received, any reduction in mortgage or any other non-like-kind property received is considered "boot" and is taxable to the extent of the capital gain. To fully defer all capital gain taxes, an Exchanger must meet two requirements:

1 REINVEST ALL EXCHANGE PROCEEDS - If an Exchanger does not reinvest all exchange proceeds from the sale of the relinquished property, the balance received is considered "cash boot," and gain may be recognized on that amount.

2 ACQUIRE PROPERTY WITH THE SAME OR GREATER DEBT - If an Exchanger does not acquire a replacement property with an equal or greater amount of debt, he or she is relieved of a debt obligation, which is considered "mortgage boot." The IRS considers this reduction in debt a benefit to the Exchanger; therefore, it is taxable, unless it is offset by adding equivalent cash to the replacement property purchase.

HOW IT WORKS

EXAMPLE 1	SALE		PURCHASE	BOOT
Sale Price	\$ 450,000	Purchase Price	\$ 600,000	
minus Debt	– \$ 200,000	New Debt	\$ 380,000	0
minus Cost of Sale	– \$ 30,000			
Exchange Proceeds	= \$ 220,000	Down Payment	\$ 220,000	0

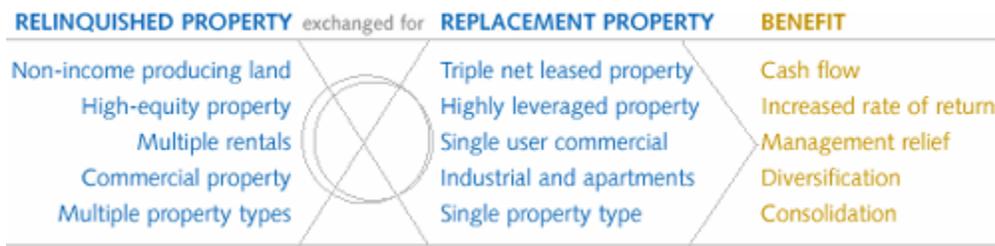
Analysis: Since the Exchanger acquired \$180,000 more debt and reinvested all the net equity, the exchange is fully tax deferred.

EXAMPLE 2	SALE		PURCHASE	BOOT
Sale Price	\$ 450,000	Purchase Price	\$ 360,000	
minus Debt	– \$ 200,000	New Debt	\$ 160,000	\$40,000
minus Cost of Sale	– \$ 30,000			
Exchange Proceeds	= \$ 220,000	Down Payment	\$ 200,000	\$20,000
Total Boot				\$60,000

Analysis: Since the Exchanger only acquired property with \$160,000 of debt, there is \$40,000 of mortgage boot. Additionally, the Exchanger did not reinvest \$20,000 of the net equity, which results in \$20,000 of cash boot. The combined amounts (\$40,000 + \$20,000) equate to \$60,000 in boot, which is taxable.

Pursuant to IRC §1031, capital gain tax deferral requires the exchange of "like-kind" relinquished property for other "like-kind" replacement property. Contrary to the commonly held misconception that exchanged properties must be of the exact same type - for example, that bare land be exchanged for bare land or an income property be exchanged for another income property - the actual definition of "like-kind" is far more empowering in its flexibility. Any real property held for investment or real property used in a trade or business can be exchanged for any other real property held for investment or real property used in a trade or business.

POTENTIAL "LIKE-KIND" PROPERTY EXCHANGES AND BENEFITS:



Property Transfer

Include verbiage establishing the intent to affect a §1031 tax deferred exchange in the Purchase and Sale Agreement. The following are examples:

SALE OF RELINQUISHED PROPERTY

"Buyer is aware that Seller intends to perform an IRC §1031 tax deferred exchange. Seller requests Buyer's cooperation in such an exchange and agrees to hold Buyer harmless from any

and all claims, liabilities, costs, or delays in time resulting from such an exchange. Buyer agrees to an assignment of this contract to Asset Preservation, Inc. by the Seller."

PURCHASE OF REPLACEMENT PROPERTY

"Seller is aware that Buyer intends to perform an IRC §1031 tax deferred exchange. Buyer requests Seller's cooperation in such an exchange, and agrees to hold Seller harmless from any and all claims, liabilities, costs, or delays in time resulting from such an exchange. Seller agrees to an assignment of this contract to Asset Preservation, Inc. by the Buyer."

WHAT IS A QUALIFIED INTERMEDIARY

In 1921, tax deferred exchanges were introduced. Since that time many significant tax law changes have taken place, the most significant being the Final Treasury Regulations of 1991, which defined the role of the "Qualified Intermediary" and streamlined the exchange process. Today, knowledgeable investors seek an experienced Qualified Intermediary to handle exchanges. The use of a Qualified Intermediary significantly reduces transactional stress by assuring the proper execution of required documentation. Qualified Intermediaries provide a vast array of options so that investors have access to the full power of exchanges.

Many investors are surprised to discover that the Qualified Intermediary industry is not nationally regulated. Consequently, the careful selection of the Qualified Intermediary is essential to ensure the highest levels of expertise and security of funds.

API provides the key services of a Qualified Intermediary as defined and required by the IRC and Treasury Regulations.

- API is a Qualified Intermediary pursuant to IRC §1031
- API confers with each Exchanger's attorney and/or tax advisor and forwards legal documentation, as requested, so that the IRC §1031 rules and regulations are thoroughly understood
- API prepares the necessary documentation - Exchange Agreement, Assignment(s), Notice of Assignment(s), Qualified Exchange Account Form, Security of Funds Instruments and Instructions to each Closer/Escrow Officer - and oversees each closing to assist in proper §1031 procedures

- API, via the proper exchange documentation, consummates the sale of the relinquished property and the purchase of the replacement property
- API holds and protects the exchange proceeds on behalf of the Exchanger until funds are needed to purchase the replacement property
- API provides guidance, information and critical timelines throughout the entire exchange

Always discuss a §1031 tax deferred exchange with your tax and/or legal advisors.

Much of the above information was supplied by Asset Management Inc. (AMI). AMI acts as a qualified intermediary (QI) in the exchange protecting the investor's assets. A QI is recommended in an Exchange. It is further recommended that you consult with your accountant and/or attorney to fully understand your tax liabilities before making any decisions

Protect Your Investment By Getting Realtor Representation

Do you remember the old riddle that goes, “*What do you call the person who graduated dead-last in their medical school class?*”

Answer: “DOCTOR!”

Well, it’s the same with Realtors. Someone with vast experience and extraordinary professionalism usually costs the same as someone with little or no experience, or with compromising standards. You need to know how to tell the difference up front.

Bringing competence and experience into your transaction may mean the difference between a higher negotiated sales price and losing money, selling in less time or in more time (costing you potentially thousands in added interest), and experiencing problems and hassles or a problem-free transaction.

Our community is loaded with Realtors who are WRONG for you, your area, and your home. Some agents are in business part time for a little extra cash. Others are subsidizing other businesses or careers. And then there’s your “*cousin Harry,*” whom you feel obligated to because he “*really needs your business.*”

Selling your home is probably the most important financial transaction you will ever make. That’s why we take my business so seriously. It’s also why we have developed customized home marketing programs meant specifically for your situation.

WHY US?

Here’s why you should consider our services to market your home:

- We are full-time Realtors. We are well educated. We have a complete resume for your review, and make it a priority to educate YOU on every aspect of your transaction.

- We have a list of references, past clients, and professional associations whom you can call at any time to discuss the quality of service we have provided to other people just like YOU.
- We have developed an EXCLUSIVE marketing plan that is unequalled by anyone in the business. We do this because our dedication to selling your home is also unsurpassed. There's no other way we can live up to that expectation without extraordinary marketing capabilities.
- We have specifically designed marketing tracking systems for every home we sell. We also have specific update systems so you are fully aware of ALL activity and progress updates on your home on a weekly basis. You will NEVER feel out of touch with US!
- We guarantee everything we do! If you're not happy with use, fire US. This places the burden of risk to perform on us, not you.
- We have references for reliable title companies, escrow companies, financing sources many agents are clueless about, insurance companies, inspectors, attorneys, and others directly relating to your transaction. If you choose to use any of them, you won't be dealing with arbitrary people. These are professionals we have used personally in other transactions.
- We schedule showings around your schedule, and to respect your personal and family time. This requires special planning and forethought most agents do not consider.
- Each day, we contact over 780 people directly related to real estate buying or selling. This allows us to create a communication link of properties to people.
- Most Importantly: We generate over 80% of my clients through referrals alone. We do very little traditional marketing. Instead, we focus our efforts into providing such outstanding service, our clients are inclined to refer our services to family, friends and acquaintances.

On the surface, it may seem there are lots of Realtors to choose from. But just because there are lots of Realtors out there doesn't mean they can all do the same job for you.

All Realtors Are NOT The Same!

We have enclosed with this report a special coupon. By simply calling 760-632-9390 We'll share with you our exclusive *Maximum Home Value Audit.* Here's what you'll get, absolutely FREE and without obligation whatsoever:

- We'll conduct a careful, thorough valuation of your home, based on real world facts, in a EASY to understand format. You won't get any inflated values just to pressure you into listing with us.

And you won't get anything like "*We have a buyer right now who's interested in your specific home, and if you list with us, I'll bring him by right now.*" With us, you'll get NO pressure. No arm twisting. Just a real world, honest, fact-filled analysis.

- We'll tour your home to identify items that could negatively affect your selling price. As mentioned earlier, many of our findings could bring as much as \$10 in extra sales price for every \$1 you invest. By the end of my tour, you'll have a checklist of strategies designed to "*position*" your home to sell for the most money possible.
- We'll share with you our *Exclusive Home Marketing Plan*. Our plan will give you insider secrets on how to promote your home properly, how to handle buyers, how to avoid crime, and much more.
- PLUS, We guarantee everything we do. If any other agent won't guarantee their services, ask them why? You're staking the successful sale of your home on their abilities, why shouldn't they stake their commission the very same way? We place our priorities in the same place as yours. We're in this together!
- When selling your home, the LAST thing you need is added pressure. That's why We'll answer all of your questions. And give you one less thing to worry about during these hectic times.

But Don't Wait!

You'll notice an expiration date for your Free Home Inspection on the attached coupon. We did this for a very good reason. We enjoy working with clients, and sometimes my practice gets booked up fast. In order to make sure we have undivided time for you, we need to hear from you immediately so there are no conflicts in scheduling our meeting.

Plus we know there's a natural tendency to procrastinate, to put off important decisions. But the more you procrastinate, the more pressure ultimately rests with you.

**By Not Acting Now, You Could Open Yourself To
Losing Thousands Of Dollars**