

Exchange Requirements

A 1031 Exchange, or like-kind exchange, is subject to various requirements and rules to qualify for tax-deferral benefits. Here are the key requirements and steps involved:

Like-Kind Property: The properties involved in the exchange must be of like kind, meaning they share a similar nature or character. Real property used for business or investment purposes can generally be exchanged for other real property.

Intent to Invest: The taxpayer must demonstrate a clear intention to hold the property for productive use in business or for investment purposes. Property held primarily for personal use does not qualify.

Qualified Intermediary: To facilitate the exchange, a qualified intermediary (QI) must be used. The QI is responsible for holding the proceeds from the sale of the relinquished property and then using those funds to acquire the replacement property.

Identification of Replacement Property: Within 45 days of selling the relinquished property, the taxpayer must identify potential replacement properties in writing to the QI. There are two common identification rules: the Three-Property Rule (identify up to three properties) and the 200% Rule (identify any number of properties as long as their combined fair market value does not exceed 200% of the relinquished property's value).

Purchase within 180 Days: The taxpayer must complete the acquisition of the replacement property within 180 days of selling the relinquished property, or by the due date of the tax return, including extensions, for the year in which the relinquished property was sold, whichever comes first.

Reinvestment of Sales Proceeds: The net proceeds from the sale of the relinquished property must be fully reinvested into the replacement property or properties. Any cash or property received that is not reinvested will be subject to capital gains tax.

No "Boot": "Boot" refers to any non-like-kind property or cash received in the exchange. To qualify for full tax deferral, the taxpayer should avoid receiving boot, or any such amounts received may be subject to capital gains tax.

Same Taxpayer: The taxpayer who sold the relinquished property must be the same taxpayer who acquires the replacement property. This means the taxpayer's name on the title must match in both transactions.

Meeting these requirements is essential for a successful 1031 Exchange and the deferral of capital gains taxes. It's crucial to consult with tax and legal professionals who are experienced in 1031 Exchanges to ensure compliance with all rules and regulations.



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