GENERAL “RULE OF THUMB”

To defer paying any capital gain taxes in an exchange, the investor should always attempt to:

1) Purchase property at a price **equal to** or **greater** than the **sales price**.
2) Reinvest **all** of the **proceeds** in replacement property (cash out will be taxed).
3) Obtain **equal** or **greater debt** on replacement property. *

***Exception:** A **reduction in debt** can be offset with additional **cash from exchanger,** but **increasing debt** will not offset **a reduction** in **exchange equity** (cash out will be taxed).*

SAME TAXPAYER REQUIREMENT

The same taxpayer(s) or taxpayer entity that owned the relinquished property must take title of the replacement property. Virtually any taxpayer or entity (corporation, partnership, trust, LLC, etc.) can complete an exchange. A good rule of thumb is to think of the taxpayer identification number or TIN (whether a social security number or a federal tax identification number). That same TIN must acquire the replacement property and report it as one exchange transaction on its tax return. There are a few situations that need special attention:

SPOUSES

If only one spouse owns the relinquished property, probably only that one spouse should take title to the replacement property. After maintaining a reasonable holding period, the other spouse can be added to the deed. If both spouses own the relinquished property, both should acquire the replacement property. For estate purposes, many taxpayers plan to have only one spouse hold title.

SINGLE MEMBER LLC’s

Many states now allow limited liability companies or LLC’s, which allow a taxpayer to be taxed as a corporation or a sole owner for tax purposes. If the taxpayer elects to be taxed as a sole owner, it is possible for the taxpayer to own the relinquished property as an individual and the replacement property as an LLC. This will satisfy the IRS same taxpayer requirement as well as the single asset entity' requirement some lenders are now imposing. It will also allow the taxpayer the protection a limited liability company provides.

Discuss your particular situation with a tax and/or legal advisor.

NOTE: Patterson Osborn Exchange Services, LLC cannot provide advice regarding specific tax consequences. Investors considering an IRC § 1031 tax deferred exchange should seek professional advice from their accountant and/or tax attorney.

DELAYED EXCHANGE DEADLINES
and IDENTIFICATION REQUIREMENTS

The most common exchange variation is the delayed exchange format. One of the central requirements in a delayed exchange is that the replacement property is properly identified within the identification period and acquired by the end of the exchange period. Treasury Department Regulations [§ 1. 103 l(k)- I (b) through (e)] clarify the acceptable methods to properly identify replacement property and the deadlines for acquiring the replacement property. Failure to comply with these rules may result in a failed exchange.

TWO KEY DEADLINES:

Identification Period: The Exchanger must identify the Replacement Property to be acquired by the end of the Exchange Period within 45 days of the transfer of the first Relinquished Property.

Exchange Period: The Exchanger must receive the Replacement Property within the earlier of 180 days after the date on which the Exchanger transferred the first Relinquished Property, or the due date (including extensions) for the Exchanger's tax return for the tax year in which the transfer of the first Relinquished Property occurs.

Note: The time periods for the 45-day Identification Period and the 180-day Exchange Period are very strict and cannot be extended even if the 45th day or 180th day falls on a Saturday, a Sunday or a legal holiday.

METHOD of IDENTIFICATION:

Replacement Property must be properly identified within the Identification Period by at least one of the following methods:

Completing the purchase of the Replacement Property within the Identification Period;

or

Identified in a written document ("Identification Notice") signed by the Exchanger and hand delivered, mailed, telecopied, or otherwise sent by midnight of the 45th day, which is the end of the Identification Period.

The Identification Notice must contain an unambiguous description of the Replacement Property and must be signed by the Exchanger. A fully executed purchase and sale agreement specifying the Replacement Property may satisfy these requirements. Otherwise, the Identification Notice must include the legal description, a street address or a distinguishable name. In addition, when the Exchanger intends to improve the Replacement Property during the Exchange Period the Exchanger must include an adequate description of the underlying land and a description in as much detail as is practicable at the time of the identification of the proposed construction or improvements.

Exchangers have the flexibility of identifying more than one property, as Replacement Property, for their exchange. The options for identification are:

Three Property Rule: The Exchanger may identify as potential Replacement Property one, two or three properties (not more than three), without regard to their fair market values.
This is the simplest and most commonly used rule. Typically three properties are named.

200% Rule: The Exchanger may identify as potential Replacement Property any number of properties provided the aggregate fair market value of all of the identified properties does not exceed 200% of the aggregate fair market value as of the date of the transfer of all of the Relinquished Properties.

95% Exception: If the Exchanger identifies more potential Replacement Properties than allowed under either the Three Property or the 200% Rules, the Exchanger must receive Replacement Property by the end of the Exchange Period that has a fair market value of at least 95% of the aggregate fair market value of all of the identified Replacement Properties. The fair market value of property is determined as of the earlier of the date the property is received by the Exchanger or the last day of the Exchange Period and without regard to any liabilities secured by the property.