



## THE 1031 EXCHANGE 180 DAY TIMELINE

**DAY  
1**

**Sell Your  
Property(s) – proceeds to QI**

**BY DAY  
45**

**Identify a  
Replacement Property(s)**

**BY DAY  
180**

**Close on Your  
New Property(s)**

To be fully tax deferred, an exchange must satisfy the following:

- **VALUE** of new RE is => **VALUE** of relinquished RE
- **CASH** invested in new RE is => **CASH** received from relinquished RE
- **DEBT** of new RE is => **DEBT** from relinquished RE

**USE DSTs TO SIMPLIFY THE 1031 PROCESS AND YOUR LIFE, PLUS HAVE THE POTENTIAL FOR MORE BENEFITS! DSTs**

reduce or **ELIMINATE BOOT** | insure 100% tax deferral | ease **MULTIPLE-Lg** property exchanges | are perfect backup ID(s) | provide more **CHOICES**  
use **PROFESSIONAL Mgt = PASSIVE INCOME** | obtain the **FINANCING** | give each heir separate options = **EASIER WEALTH TRANSFER**

Or get up to **86%\* of cash portion cash now**, tax-free, (14% deferred in a DST) from the 1031 sale of relinquished property

**\$1M of equity 1031ed into a DST could yield \$50K annually + growth, which transfers to heirs (fractionally) all without Capital Gains Tax and without management or maintenance headaches.**

- 1. They Avoid Financing Obstacles** - Since debt placed or assumed on the replacement property must be equal to or greater than the debt relieved in the relinquished property, property owners may have difficulty getting financing on their replacement properties. For example, a property owner may wish to sell an apartment building worth \$5 million with 50% loan-to-value (LTV). If that property owner cannot get approved for a \$2.5 million loan on their replacement property, then most likely the owner will not sell. The DST(s) can be the borrower of any loan and investors in that DST will not need to be individually qualified with a lender. The debt is non-recourse to the investors.
- 2. DSTs Make Great, Reliable Back Up Properties** - A common strategy to identify replacement properties is the “3 Property Rule,” where an exchanger may identify up to three properties, without regard to their fair market value, within 45 days. Identifying only one property may be dangerous because that property can fall out of escrow for many reasons: financing, inspections, seller changes their mind, etc. It costs the exchanger no extra money to identify additional properties. Taking this precaution ensures that the exchanger has adequate choices since DSTs will not fall out of escrow.
- 3. They Avoid Taxable Gains on Boot** - The exact dollar amount of the replacement property is a common challenge in 1031 transactions. In one example, the relinquished property sells for \$2M and the exchanger identifies a replacement property for \$1.8M. The difference in the price of the relinquished property and the price of the replacement property results in a taxable amount on the remaining \$200,000. Under the “3 Property Rule,” DSTs provide a solution by identifying the extra \$200,000 as DST owned properties. And DSTs **avoid Time Constraints**
- 4. No Property Management Headaches** - DST-structured 1031 exchange properties are professionally managed. Professional managers handle the Terrible T’s: Tenants, Toilets, Trash, Turmoil, Termites. The investor enjoys the Terrific T’s: Travel, Time, Tennis. DST programs offer additional benefits, including the direct deposit of distributions, if any, and reporting through Substitute 1098/1099s, no K-1s.
- 5. New Depreciation** - more real estate value and higher basis to depreciate.
- 6. DSTs Give Investors More Choices & Diversification** - Investing in a DST can provide portfolio diversification. For instance, an investment could be made in a single DST that owns multiple properties in several states. It would be almost impossible for a broker to identify three replacement properties in three different states within the allowed 45-day timeframe. DSTs are an optimal way to achieve diversification and to give investors more choices.
- 7. They Don’t Get Sidelined** - Many realtors have clients that will not sell until they find the “right” property. Having the option to invest in institutional-grade properties, owned by professionally managed DSTs, may get investors off the sidelines, allowing realtors to make more sales.
- 8. Swap till You Drop and Estate Planning Tool** - A DST is different than a 721 Exchange (UPREIT) transaction where the investor’s exchange opportunity for heirs to argue over what to do with an investment property when the owner passes away. The heirs continue to receive distributions from the investment, if any, and upon the sale of the property owned by the DST, each of the heirs can choose what to do with their inherited portion of DSTs (DSTs can be fractionalized to different heirs). One heir can continue to exchange the investment, without stopping at the sale of the UPREIT. The DST structure allows the investor to continue to exchange properties repeatedly until the investor’s death. Upon the death of the investor, under current tax laws, the heirs would get a “step up” in basis, thereby avoiding capital gains taxes on the original and subsequent properties.
- 9. Low Minimums** - An investor can exchange as little as \$100,000.

# Three Property Identification Rules

A person engaging in a 1031 Exchange must identify the replacement real property through ONE of the following three rules:

- 1. Three Property Rule:** An exchanger may identify up to **three** replacement properties, **regardless** of their fair market value (“**FMV**”); or,
- 2. 200% Rule:** An exchanger may identify **any number** of replacement properties as long as the **combined FMV** of those properties does **not exceed 200%** of the FMV of the relinquished property (i.e., the real property the exchanger is selling); or,
- 3. 95% Rule:** An exchanger may purchase **any number** of replacement properties, with no limit on FMV, as long as the properties acquired amount to **at least 95% of the FMV of all identified properties.**

- 1. \*** Sell commercial propert(ies) as a 1031, No-Boot transaction, replaced by a long-term DST using a fortune 100 tenant.
2. 30 days after the completed 1031 transaction, ReFi at 86% loan-to-value
  - a. Non-recourse debt (because loan is unwritten to the fortune 100 tenant and property), without amortization costs (because rent income makes the loan payments), all tax-free debt
  - b. Remaining 14% is deferred in the long-term DST
  - c. Paid fixed \$7,500 legal fee
  - d. Any debt is paid off from ReFi proceeds.
3. Examples: \$10M sale, no debt = \$8.6M cash now | with 30% debt = \$5.6M cash now

## 1031 TERMS

**Accredited Investor** - Defined in Rule 501 of Regulation D. While each state may have additional accreditation requirements, individuals are generally considered to be accredited if they have a net worth exceeding \$1,000,000 (not including value of primary residence), or if their income exceeds \$200,000 in each of the last two years. A joint income with a spouse exceeding \$300,000 for those years with an expectation of the same income level in the current year.

**Basis** - The value of a property for tax purposes. Takes into consideration added value for capital improvements and decreased by the amount of depreciation taken.

**Boot** - The money or the fair market value of “other property” received by the taxpayer in an exchange. Subject to taxation to the extent there is a capital gain. Examples of boots can include cash boot, mortgage boot, and personal property.

**Exchange Period** - The time frame in which the exchanger must acquire the replacement property in the exchange. Starts on the date the exchanger transfers the first relinquished property and ends when the exchange is completed or on the 180th day.

**Exchanger** - The property owner aiming to defer capital gain by utilizing a 1031 exchange.

Forward Exchange - Most common form of a 1031 exchange. Begins with the sale of the relinquished property and completes with the purchase of a replacement property.

**Identification Period** - The 45th period in which the investor must identify up to three potential replacement properties for a like-kind exchange. The 45-day window begins with the transfer of the investor’s relinquished property.

## 1031 TERMS continued

**Like-Kind Property** - Any real property held for productive use in a trade or business or for investment can be considered “like-kind” property. Any real estate that is not help for personal use.

**Private Placement Memorandum (PPM)** - A legal, offering document that contains relevant objectives, disclosures, risks, and terms to aid investors in making informed investment decisions. May include financial statements, details of the company or entity issuing the securities offered, and the procedures for investing. Sometimes referred to as offering memorandum or offering document.

**Qualified Intermediary** - Third party entity that holds the exchanged funds and helps facilitate the exchange. Also referred to as QI, exchange facilitator, or exchange accommodator.

**Realized Gain** - Amount of the realized gain that is subject to tax. In a fully tax-deferred 1031 exchange, no gain is recognized.

**Relinquished Property** - The property the exchanger is selling.

**Replacement Property** - The property the exchanger is acquiring (purchasing).

**Reverse Exchange** - A 1031 exchange in which the replacement property must be purchased before the relinquished property is sold. It can also take place when improvements must be made to the replacement property before it can be acquired by the exchanger. Generally, more complex than a forward 1031 exchange.

**Sponsor** - The company/party offering a property asset is available for sale to investors. The sponsor handles everything from purchasing the property, to building the financials, to handling of the property management. The sponsor will sell fractionalized interests to individual investors.

## **General Disclosure**

The contents of this communication do not constitute an offer of securities or a solicitation of an offer to buy securities. You should always consult a tax professional prior to investing. All investing involves risk.

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## **1031 Risk Disclosure:**

- There is no guarantee that any strategy will be successful or achieve investment objectives;
- Potential for property value loss – All real estate investments have the potential to lose value during the life of the investments;
- Change of tax status – The income stream and depreciation schedule for any investment property may affect the property owner's income bracket and/or tax status. An unfavorable tax ruling may cancel deferral of capital gains and result in immediate tax liabilities;
- Potential for foreclosure – All financed real estate investments have potential for foreclosure;
- Illiquidity – Because 1031 exchanges are commonly offered through private placement offerings and are illiquid securities. There is no secondary market for these investments.
- Reduction or Elimination of Monthly Cash Flow Distributions – Like any investment in real estate, if a property unexpectedly loses tenants or sustains substantial damage, there is potential for suspension of cash flow distributions;
- Impact of fees/expenses – Costs associated with the transaction may impact investors' returns and may outweigh the tax benefits