The Real Estate Exchange Company

Realty Exchangers, Inc.®

Qualified Intermediaries for Section 1031 Exchanges since 1990

Tax Alert Newsletter

July 15, 2002 - VOL. 1, NO. 19

http://www.1031help.com

Realty Exchangers Tax Alert is a FREE biweekly newsletter published by Realty Exchangers University as a part of their exceptional educational program for the real estate community.

Recognizing that federal taxation issues are the main driving force behind completing a successful exchange, Realty Exchangers, a QUALIFIED INTERMEDIARY for Deferred Exchange transactions, is proud to publish this E-Letter to keep you right on top of current developments and tax planning ideas.

In This Issue

We understand exchanges and maintain one of the largest information databases to help you. Whether you're in need of our services as your Qualified Intermediary, or just have questions, please call us (1-800-570-1031). Talk with us. Or visit our home page at http://www.1031help.com

If you have 1031 questions or would like to comment on our newsletter, please eMail our tax consultant: askrich@commspeed.net

---

Announcements

back to index

Many readers have asked where can they find past copies of this News Alert Letter. Click on http://www.realtyexchangersuniversity.com/2-

TaxAlertArchives.htm where you will find the last four issues.

You will also find a Go Link to our Archives where information reported in previous issues has been classified and posted by subject, such as 1031 Exchanges, Farm and Land, Rental Properties and so forth. To keep on the cutting edge of tax issues related to real estate transactions, you should check this site often as new information is posted weekly.

Tax News

back to index

President Bush Promotes Home Ownership Tax Credit.

On June 17, President Bush promoted plans to provide developers of single-family homes in qualified areas with tax credits worth up to 50 percent of the qualifying costs of new units.

The President backed the plan to develop a new single-family housing tax credit during the 2000 presidential campaign and included it in his fiscal 2002 and 2003 budgets. His proposal would provide developers of new or rehabilitated single-family housing in census tracks with median incomes of 80 percent or less of area median income with tax credits worth up to 50 percent of the qualifying costs of that unit. The initiative would go into effect beginning in fiscal 2003 and is backed by the National Association of Realtors.

Jim Maxwell on Title Issues in 1031 Exchanges

back to index

One of the vital tax concerns presented in structuring a 1031 real estate exchange is the issue of title. Almost all exchanges require the exchanger to take title to the Replacement Property in the mode the exchanger held title on the Relinquished Property. In other words, the same entity commencing the exchange must be the same entity receiving the Replacement Property and concluding the exchange. For example, if an individual owns the Relinquished Property, then the same individual owns the Replacement Property (however, see exception below for marrieds); ABC Corporation relinquishes and ABC Corporation acquires; XYZ Partnership relinquishes and XYZ acquires.

Anytime the vesting title is different in the Relinquished Property and the Replacement Property, you should consult your attorney before entering into the exchange agreement. For example, if an individual taxpayer owns the stock in a C Corporation, and the Corporation owns the Relinquished Property in an exchange and the Replacement Property is taken in the name of the individual taxpayer, 1031 exchange treatment is denied. In fact, the taxpayer has a severe problem of taking a distribution from the Corporation, which could be classified as dividend income with no deduction allowed to the Corporation.

Like most tax rules, there are some special exceptions. One of the most important applies to individuals who are married to each other. In a 1031 exchange, spouses can be added or not added to transfers of title interests without jeopardy. For example, The Relinquished Property is held in the name of John Smith who is married to Sue Smith. Sue's name is not on title. They take title to the Replacement Property in both names. Or, the other way around.

Other Exceptions:

1. If the exchanger dies after the exchange is commenced but before it's completed, the exchanger's estate may complete the exchange.
2. There is a special rule that permits an individual who holds title to the Relinquished Property to relinquish that property in exchange for Replacement Property vested in the name of a single-member, single-asset LLC.

Exchange Workshop

back to index

Rules for Relinquishing Two Properties for One Replacement Property in the Same Exchange.

Sometimes in a deferred 1031 exchange, you transfer more than one Relinquished Property and they are transferred on different dates. If this happens, the 45-day Identification Time Period and the 180-day Exchange Time Period are measured from the earliest date on which any of the properties are transferred. Not following this rule can cause your exchange to end in disaster.

All the other rules and requirements spelled out in the Regulations apply in the usual manner. You simply combine the numbers from the sale of both Relinquished Properties and following the tax accounting rules, apply them to the exchange for the Replacement Property.

Illustration: You enter into an exchange agreement with your Qualified Intermediary. As part of the exchange transaction, you are selling two Relinquished Properties and acquiring one Replacement Property. You sell Property One on July 1, 2002 for $150,000 with terms of $30,000 cash and the buyer assumes your mortgage of $120,000. You sell Property Two on July 21, 2002 for $200,000 with terms of $130,000 and the buyer pays off your mortgage of $70.000.

This entire set of transactions is treated by IRS as one exchange transaction. Your 45-day Identification Period for both properties starts on July 1, 2002. To successfully qualify for exchange treatment on both properties, you must identify the Replacement Property within this 45-day period. To qualify for complete non-recognition of gain, you must "invest" at least the $160,000 cash proceeds in the Replacement Property plus off-set $190,000 of mortgage relief boot. It's just a matter of adding the numbers of both sales together to determine the financial requirements for the purchase of the Replacement Property.

(For detailed information on Identification and Exchange time periods, see http://www.realtyexchangersuniversity.com/PI-H-4-TimePeriods.htm)

Questions and Answers

back to index

1. **Question from Alan** - Hi, Thanks for the opportunity to pose a real times question to you.

   My client, the Exchangor has closed on the sale of the relinquished property and has identified a replacement property that is under construction. The builder represents that the replacement property will be issued a Temporary Certificate of Occupancy and will close within the 180 day closing requirement. What is the impact for the transaction if the builder is late in acquiring the C of O and that the replacement property may only be completed after the 180 day window. Are there additional rules for this type of scenario?

   Realty Exchanger's Answer - Hi Alan - If at the end of the 180 day exchange period, the property is not completed, the builder can deed over the property "as is" (before the 180-days) and the cost of the property at that time will count as qualified property of like-kind. Any costs added after that date will count as boot received. If you are "trading up", then it is possible the cost at the time of transfer will be more than enough to qualify you for a full 1031 benefit. It's a matter of crunching the numbers.

   Take a look at http://www.realtyexchangersuniversity.com/PI-H-4-TimePeriods.htm#11%20-%20Replacement%20Property%20to%20be%20Produced

   Produced on our University Web site for more information on this subject.

2. **Question from T** - I work for the state of ____. There are agricultural easement programs where easements are placed on farmland. Can the farmer take the money from the easement do a 1031 exchange to buy another farm?

   Realty Exchanger's Answer - The sale of an easement gets special treatment under federal tax rules. It works like this: The sales price of an easement is not treated as income. Instead, it reduces the basis of the underlying land. If the sale price of the easement is more than the cost basis of the entire parcel of land, the difference is treated as long-term capital gain and the farmer has a zero-basis in his farmland.

   Example: You are a farmer and your farmland has a federal tax basis of $100,000. You sell an easement to the power company (or anyone) for $6,000. You pocket the $6,000 tax-free and the cost basis of your farmland is reduced to $94,000.

   This is a mandatory rule so the farmer can do anything he wants with money.

   As you can see, this is a great tax benefit and farmers all over should know about it.

Tax Idea

back to index

Let's take the sale of easement example and develop it one step more. In the example, the landowner pockets the $6,000 easement money as nontaxable income. Since it reduces the basis of the land, this results in an additional $6,000 gain when the property is sold. But instead, the landowner sells the land in a deferred 1031 exchange. And eureka! The "extra" $6,000 gain is still not recognized since it rolls into the substituted basis of the Replacement Property.

About Realty Exchangers, Inc.

back to index

Realty Exchangers, Inc. is a **QUALIFIED INTERMEDIARY** for Deferred Exchange transactions and specifically structured to assist Exchangers and Real Estate Professionals in effecting successful IRC '1031 Deferred Exchanges. We fully understand the real estate transaction, the needs of the investor, and the technical requirements of the IRS. Realty Exchangers, Inc. can initiate documentation for delayed exchanges with as little as two hours notice and furnish all the paperwork and necessary forms. We also consult with real estate professionals, tax consultants, and legal advisors involved in the exchange. We are dedicated to providing the fastest and most accurate service available.

Now in our twelfth year of providing fast and accurate service to all fifty states and the U.S. Virgin Islands, we are fully computerized and process all of our transactions by electronic transfer. Wherever you're located we're as close as your phone. Whether you're in need of our services as your Qualified Intermediary, or just have questions, please call us (1-800-570-1031). We'll be happy to hear from you and help you in any way we can.

Important Links

back to index

- Visit our site at http://www.1031help.com
- For a great new library of 1031 information, visit http://www.realtyexchangersuniversity.com/2-procmanual.htm
- Visit the REU Bookstore at http://www.realtyexchangersuniversity.com/1-bookstore.htm
- For a review of the new Realty Exchangers 1031 Exchange Manual, aim your browser at http://www.realtyexchangersuniversity.com/2-

procmanual.htm

- If you have 1031 questions or would like to comment on our newsletter, please E-mail askrich@1031university.com/

- Visit the REU On-line campus at http://www.realtyexchangersuniversity.com where we have added lots of new material and information regarding 1031 deferred exchanges.

Contact/Address Change/Removal Information

back to index

This FREE twice-per-month Email Newsletter is submitted to you as a Real Estate Professional who wishes to stay on the cutting edge of real estate tax issues in order to provide exceptional service to your clients.

Removal: If you would like to be removed from our database, please send an email message to the following email address with REMOVE in the subject line. ***Don't forget! Include in your message the email address this message was sent to.***

remove@1031university.com

Change/Update: If you would like to change your email address, please remove your email address from our database by clicking the above link, then re-add your corrected email address at

http://www.1031help.com

This taxation news letter comes to you as a service of Realty Exchangers as part of our continuing education program for the real estate community. While designed to provide accurate and authoritative information, it is not meant as a substitute for your own CPA, professional tax advisor, or attorney. Tax planning depends on your individual facts and circumstances. You should always consult with your own tax advisor to determine if the ideas and techniques discussed here apply to your situation.

REALTY EXCHANGERS TAX ALERT
Brought to you by Realty Exchangers, Inc.
A Qualified Intermediary Company since 1990.
http://www.1031help.com

Edited by James D. Maxwell