

# **SECTION 1031**

# **EXCHANGE HANDBOOK**

**Olympic Exchange Accommodators, LLC**

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**FEE SCHEDULE**

All fees include one free initial consultation, errors and omission insurance, and the advantage of experienced lawyers overseeing your exchange. Unlike many accommodators, our banking partners pay you directly the interest on your exchange balance. In addition, Qualified Escrow Accounts are also available to you for additional protection.

**Typical Forward Exchange Fees**

Up to \$500,000.00 . . . . .	\$2,500.00
From \$500,000.00 to \$1 million . . . . .	\$3,000.00
Above \$1 million . . . . .	Contact us for quote

**Additional Fees**

More than one sale or replacement property leg \$ 250.00 per leg  
All interest earned accrues and is paid to you.

**Reverse Exchange . . . . .** Contact us for quote

By its nature a reverse exchange will add cost to your exchange because of the additional legal and accounting work that is required; however, you will find our fee to be modest and highly competitive. The specific fee will depend on the complexity and length of your reverse exchange. Please call for a prompt quote.

**Improvement Exchange . . . . .** Contact us for quote

Like reverse exchanges, improvement exchanges are more complex and individually unique and also require additional legal and accounting work to maximize the benefit to you. Our fees, you can be assured, are always very competitive with any in the industry and more importantly, the quality of our work is above comparison. We invite you to call for a quote on your improvement exchange.

**Contact us at:**

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## HOW TO SELECT AN EXCHANGE ACCOMMODATOR

*In the overwhelming majority of states, there are no licensing requirements for Exchange Accommodators, and few regulations on who can serve as one. Therefore, it is crucial to select an Exchange Accommodator with professional credentials and extensive experience.*

### **Documentation**

The Exchange Accommodator is responsible for putting the documentation in place to qualify your transaction as a 1031 Exchange. That documentation must be in place before the closing on the sale property. There are typically three documents the Exchange Accommodator will provide: the exchange agreement, an assignment, and a notice.

The exchange agreement is a contract between you and the Exchange Accommodator that sets out the rules you must follow in order to complete the 1031 Exchange.

The assignment of the sales contract to the Exchange Accommodator must also be in place. Remember that you cannot have control of the proceeds or the actual receipt of the money. The assignment allows the Exchange Accommodator to receive the proceeds for you.

The Exchange Accommodator will provide a notice to the party on the other side of the transaction advising that the transaction is a 1031 Exchange. The purpose of notification to the other party is to prove that the exchange was in place at closing.

### **Insurance**

We have errors and omissions insurance coverage.

### **Security of your Funds**

We have set up very specific protections for the safety of your funds with our banking partners. All accounts are set up separately from any other clients' exchange funds. In addition, protections include: (1) dual signature requirement to move any funds so that you must sign all wires, (2) On-line access to view your account information, so that you can see your current balance and activity, (3) establishment of a Qualified Escrow Account with our banking partners as Escrow Holder, requiring them to verify and check all signatures on all wires.

Security of your money is Priority Number 1.

## **Member of FEA**

We are active members of the Federation of Exchange Accommodators (FEA), the only national organization for Exchange Accommodators.

## **Knowledge and Professionalism**

Olympic Exchange Accommodators, LLC is proud to have Mr. Helsdon on staff. Jeffrey P. Helsdon is the first Certified Exchange Specialist® in the South Puget Sound area of Western Washington. Mr. Helsdon was one of the first Exchange Accommodators to receive the CES® designation from the Federation of Exchange Accommodators, the national trade association for exchange accommodators, of which Olympic Exchange Accommodators, LLC is a proud member.

Expect your Exchange Accommodator to answer questions about your exchange at no charge to you. Your Exchange Accommodator should have real estate, tax, and legal professionals on staff, ready and able to answer even the most complex 1031 questions. Questions to ask of a prospective Exchange Accommodator include:

### **How are the Exchange Accommodator's fees structured?**

Many Exchange Accommodators charge a front-end fee when you sell your old property and an additional back-end fee when you buy your new property. Some also charge an additional set-up fee and some charge a monthly holding fee. When you inquire, make sure you understand the total costs of your exchange.

### **Who earns interest on the exchange funds?**

In many cases, it is the Exchange Accommodator. We do not. All of our exchange clients earn the interest on the funds held during the exchange.

## **An Exchange Timeline**

### **Phase I: Sale of Old (Relinquished) Property**

#### **A. Contract Stage**

1. Negotiate and sign your contract as seller.
2. Include language in your contract to establish your intent to do a tax deferred exchange:

*“Seller intends to do a 1031 Exchange and buyer agrees to cooperate with seller regarding the exchange at no additional cost to buyer and no delay to the closing”.*

3. Select a title company and/or closing agent to handle the closing of your transaction.

#### **B. Closing Stage**

1. Call OLYMPIC Exchange Accommodators, LLC (OLYMPIC) when you have a signed contract. Information we will need:
  - Phone number, name, and reference number for your closing agent or title company and a copy of your contract
  - Your mailing address, phone and fax numbers
  - Sale price of the property you are selling
  - Amount of any debt on the property you are selling
  - Percentage of ownership of the property you are selling (i.e., if you own half of the property)
  - Whether you are going to help the buyer of your property finance the purchase (i.e., owner carry)
  - In what name you hold title to the property
  - If you need any cash out of the transaction (this amount will be taxable boot to you).
2. Olympic Exchange Accommodators, LLC will contact the closing agent or title company and will prepare the exchange agreement between you as an Exchangor and Olympic Exchange Accommodators, LLC.
3. The exchange agreement will be forwarded to you or to the closing agent, depending on timing and the location of the closing. Draft copies of the exchange agreement may be forwarded to you if time allows.

4. The sale closes, and funds from the sale are wired or delivered via check into your exchange account with Olympic Exchange Accommodators, LLC.

## **Phase II: Purchase of the New (Replacement Property)**

### **A. Identification Stage**

1. You have exactly 45 days (including Sundays and holidays) from the closing of the old property to identify a list of possible replacement properties and 180 days to purchase one or more of those properties.
2. From the time you decide to do an exchange, you should be looking for your new property. If you haven't started looking yet, you must begin earnestly seeking new properties NOW.
3. For an exchange to be 100% tax deferred, you must acquire new property that is of equal or greater value than the old property; you must also spend all of the net proceeds from the old property in purchasing your new property.
4. Olympic Exchange Accommodators, LLC will send you a notice containing the original closing date, the expiration date of the 45-day identification period, the expiration date of the 180-day purchase closing date, confirmation of the amount we received from your closing on the old property, and a form by which you notify us of the locations of potential new properties.
5. You must mail or fax to Olympic Exchange Accommodators, LLC the property identification form before midnight of the 45<sup>th</sup> day from the closing of the old property.

### **B. Contract Stage**

1. Negotiate and sign your contract as buyer on the new property.
2. Include language in the contract to establish your intent to do a tax deferred exchange:

*“Buyer intends to do a 1031 Exchange an seller agrees to cooperate with buyer regarding the exchange at no additional cost to seller and no delay to the closing”.*

3. Identify a title company or closing agent to handle the closing of the transaction.

### **C. Closing Stage**

1. Call Olympic Exchange Accommodators, LLC when you have a signed contract to buy. Information we need includes the phone number, name, and reference

number for your closing agent or title company, a copy of your contract and the purchase price.

2. Let Olympic Exchange Accommodators, LLC know if you need an earnest money deposit from your exchange account.
3. Olympic Exchange Accommodators, LLC will wire or deliver to closing the funds necessary to close on your purchase. Olympic Exchange Accommodators, LLC will contact the title company or closing agent with the necessary documents. If possible, a representative of Olympic Exchange Accommodators, LLC will be present at closing to obtain signatures on documents.
4. Olympic Exchange Accommodators, LLC's Exchange Tracker packet provides a final letter and an accounting of the funds held, interest calculations and the 1099 IRS form required for tax purposes.

Olympic Exchange Accommodators, LLC makes every effort to simplify the 1031 process. We complete all the necessary documents and tax requirements giving you the confidence that your exchange has been completed correctly. We know you will appreciate our service. We specialize in customer satisfaction.

For the Olympic Exchange Accommodators office nearest you call: **253-512-1031**

**Toll free: 866-309-1031**

# 1031 EXCHANGE HANDBOOK

## DOES THIS SALE QUALIFY?

### HOW TO DETERMINE WHETHER YOUR REAL ESTATE SALE COULD BE A 1031 EXCHANGE.

What did you do with the real property you are selling? If the real property has been held either for productive use in your trade or business, or for investment, it may qualify for non-recognition of the gain realized from the disposition of the property under Section 1031.

## HOW DOES A 1031 EXCHANGE WORK?

The first requirement for a 1031 exchange is that the property must be real property. Both the real property to be disposed of and the new real property to be purchased be like-kind. This is one of the most misunderstood concepts in 1031 exchanges. Like-kind relates to the use of the properties. Any real property used for productive use in a trade or business or for investment qualifies as like-kind to other real property held either for productive use in a trade or business or for investment. You can dispose of a rental duplex to buy a strip mall. You can dispose of a warehouse and buy a condominium that you intend to hold for investment. In addition, raw land held for investment qualifies for 1031 treatment whether or not you had it leased.

### Example 1:

Bill and Linda own a duplex they bought in 1986 and have rented it out ever since. They want to sell it and buy a condominium in Hawaii to rent out to others. Does this qualify as a 1031 exchange? Yes, both properties are held for income or investment purposes.

### Example 2:

Bill owns an office building that he leases to other doctors. Can he exchange the building for a piece of raw land on which to build an apartment building that he will hold for the rental income? Yes, investment property can always be exchanged for raw land held for income or investment purposes.

## THE 45 DAY IDENTIFICATION RULE

The Internal Revenue Code requires that you identify replacement properties within 45 days of the closing on the sale of the old property. The 45 days are calendar days so if the 45th day is Sunday, Christmas or the Fourth of July, that day is still the deadline for identification of new properties. No extensions are allowed. There are two ways to comply with the 45 day identification requirement. The first way is to have already purchased your new property. If you can use all your money from the sale (your exchange proceeds) your exchange is complete at that point.



In the event that you haven't closed on a new property and spent all the money within 45 days, you must identify your new property. By midnight of the 45th day you must compile a list of properties that you are thinking about purchasing to replace the property you just sold. The list must be specific. It must be in writing. It must show the property address, the legal description, or other means of specific identification. It must be signed by the taxpayer. This identification list must be presented to a person who is involved in the exchange before the deadline.

You can identify up to three potential new properties without regard to the value of the properties on the list. If you wish to identify more than three potential replacements, the IRS requires that the total value of everything identified be less than double the value of the property or properties sold. This is called the two-hundred percent (200%) rule. You may identify more than three possible replacements but be aware of the two-hundred percent (200%) rule. A third manner of identification exists, which is referred to as the 95% rule. In this rule, you can identify more than three potential replacement properties whose value is greater than twice the value of the relinquished properties, but if you do, you must acquire properties on the list whose value is at least 95% of the value of all of the properties on the list. Few people will attempt to qualify their transaction under the 95% rule.

If you wish to change the identification statement, you may do so until the expiration of the 45th day. After that date, it is not possible to change the identification. You must acquire at least one of the properties on the list that exists by day 45.

Example 1:

Jane sells her old property for \$100,000 on January 1. She may identify up to three new properties of any value within 45 calendar days of January 1.

Example 2:

Jane sells her old property for \$100,000.00. Jane wants to identify four potential new properties; four condominiums selling for \$75,000 each. Is this okay? Answer, no, the four properties identified exceed two-hundred percent (200%) of the value of the property sold.

## **THE 180 DAY RULE**

Section 1031 requires that you purchase one or more of the new properties by the 180<sup>th</sup> day after closing of the old property, or the date that your tax return falls due for the year of the Relinquished Property together with any extensions, whichever shall occur first. You must purchase one or more properties listed on your 45-day identification list. You cannot buy new property not listed.

Example 1:

Brad identified only one property, a condominium under construction, within 45 days of his sale, but now the builder tells him it won't be completed and ready to close within the 180-day period. If Brad cannot close within 180 days his exchange will fail.

### Example 2:

Katie Tierney closes her Relinquished Property on December 31, 2005. Her 2004 federal income tax return is due on April 15, which is 105 days after her Relinquished Property closed. Katie cannot close her Replacement Property until May 30. For Katie to close her Replacement Property, she must file an extension of the time to file her federal income tax return, in which case she has until August 15 to file her return. She therefore has her full 180 days to close her Replacement Property and can close it on May 30.

## **QUALIFIED INTERMEDIARY**

The most commonly used safe harbor in Section 1031 exchanges is the use of a Qualified Intermediary (QI). The term Exchange Accommodator (EA) is also used in the industry to identify the function. The EA cannot be someone with whom you have had a business or family relationship. Thus, for example, your attorney, accountant or your brother are all disqualified. You must use an independent organization whose only contact with you is to serve as the EA. The EA prepares the exchange documents, holds the cash proceeds from the sale and should answer any questions you may have during the exchange. The EA must hold your proceeds from the sale of the property in order to have the transaction qualify as a 1031 exchange. If you have actual or even constructive possession of the proceeds (i.e., control of the money without actual possession) this transaction is taxable to you. If and when you determine that you want to undertake a 1031 exchange, you must involve the EA prior to the closing of the sale of your current property.

You should be aware that there is very little, if any, government control over the qualification of an EA. It is important then that you be aware of the history, reputation and experience of the organization you choose to act as your Exchange Accommodator. It is also important to be certain that this organization is both bonded and insured. Olympic Exchange Accommodators, LLC meets all of these qualifications and more

## **TITLE REQUIREMENTS**

Section 1031 requires the taxpayer on the old property be the same taxpayer on the new property. Examples of entities holding property are trust corporations, partnerships and LLCs. If ABC partnership is in title to the old property, ABC partnership must take title to the new property. If you and your spouse hold title to the old property, you and your spouse must take title to the new property. However, a husband and wife who are the sole members of an LLC holding qualifying property in a community property state, and who file their tax return jointly, are deemed to be a single member of the LLC. Since the LLC entity is disregarded for all purposes under the Internal Revenue Code when owned by a single member, a husband and wife in this situation may take title to the Replacement Property in the name of an LLC that they solely own.

### Example 1:

Bill owns a rental building in his own name but wants to buy a new property to be held in the name of a new corporation that he wants to set up. Can he do this? No, he must acquire the new property in his own name to complete this exchange.

### Example 2:

George who is married to Jane owns a duplex that is titled in his name alone. Can he take title in the new property in his and Jane's name? No, George must first complete his exchange in his own name. In the alternative, he may take an undivided interest in the property (i.e., Bill as to an undivided fifty percent (50%) interest) to complete his exchange and Jane can take the other fifty percent (50%) interest. This will only work if Bill's purchase of the fifty percent (50%) interest will allow him to spend all of his exchange proceeds and trade equal or up in value.

## **EQUAL OR GREATER INVESTMENT**

The last rule under Section 1031 is that in order to defer one-hundred percent (100%) of the taxes on your gain from the sale of old property you must buy equal or greater in value than what was sold. There are two aspects of the rule. First, you must buy a property or properties that have equity equal to or greater than the equity of the property sold. Second, the debt incurred on the purchase of the new property must be equal to or greater than the debt on the property sold.

Can you take money out of the deal at closing? Yes, this money (called boot by the IRS) is taxable, but can be taken out of the exchange without invalidating the rest of the exchange if the exchange documents so provide. You would simply pay tax on the boot taken.

### Example 1:

Pete owns a property he is selling for \$200,000. He has a \$75,000 mortgage against the property. He wants to buy new property for \$125,000 with cash. Is this a fully tax deferred exchange? No, Pete is buying down from \$200,000 to \$125,000. Pete owes tax on the amount for the buy-down (i.e., \$75,000).

### Example 2:

As in the example previous, George decides to buy a property for \$250,000 by getting a loan for \$150,000 and using \$100,000 of the \$125,000 cash the EA is holding. Is this exchange fully tax deferred? No, George did not use all the cash the EA was holding.

## **TIMING**

The IRS requires that an exchange be completed before filing of the tax return for the tax year in which it was begun. This means a taxpayer who begins an exchange after October 31 and if they intend to use the full 180 days to complete their exchange, they will need to

file for an extension of their tax return from April 15 to August to obtain the use of the full 180 days.

## **EXCHANGES OF A MORE ADVANCED NATURE**

### Common Ownership Problems

Any tax paying entity can do a 1031 Exchange including C Corporations, S Corporations, partnerships and limited liability companies. Remember the taxpayer on the old property must be the same taxpayer on the new property.

One common ownership problem is that owners often don't know how they hold title to the property. If two or three people own a property, they may hold title to the property as tenants-in-common, but still be deemed a partnership for federal income tax purposes. A taxpayer may not exchange into or out of partnership interests.

Another common ownership problem arises when an investment property is owned by a partnership, an LLC or corporation. The decision has been made to sell the investment property, and some of the partners wish to do an exchange, while others wish to take the cash. In this situation, a well-intentioned attorney or CPA may advise dissolving the entity so that each owner can choose his own course of action. This may not be sufficient, however. If the entity is dissolved before the exchange, the IRS could argue that the property was not held by the former partners, members or shareholders for investment, since it was held in their name for only a few days from the time it was distributed to them.

Ownership issues can be a real minefield for an exchange. Please call Olympic Exchange Accommodators, LLC before you enter the exchange process for individualized consultation. If you are contemplating a partnership split-up, our lawyers can assist you.

### Refinancing the 1031 Property

There is a risk to refinancing the property to be sold because the IRS has ruled that cash proceeds refinanced immediately prior to closing in the exchange constitutes taxable boot. The rule of thumb in refinancing before the exchange is: don't. You can refinance the new purchased property immediately after the exchange is completed.

### Owner Carried Financing in 1031 Exchanges

If you carry back a note on your sale property the IRS will treat this note as taxable. As the payments on the note come to you, the principal portion of the payment is subject to capital gains tax and the interest portion is subject to ordinary income tax. How can you prevent this note from being taxable? First, the note should be payable to the EA which puts the note in the exchange. The note must first be converted to cash before you can buy the new property. How do you turn the note into cash? There are three ways. Number 1 is to get the seller of the new property to agree to take the note as part of the purchase of the new property. As a practical matter, you almost never see this. Number 2 is to find someone to buy the note. Unfortunately, because the note is unseasoned (i.e., is a brand new note) any buyer of that note would demand a large discount.

Number 3 is that you, as the property seller, buy the note from the EA for face value and the EA assigns the note back to you. Because you bought the note from the EA at face value as you receive the principal payments they are tax free return of basis to you. You will pay income tax on the interest on the note as you receive it, but the principal payments are tax free. Meanwhile, in your exchange account the EA is holding the cash that you now can use to purchase the new property.

### Reverse Exchanges

What if you want to buy your new property before selling your old property? If you buy the new property in your name and subsequently sell the old property, the transaction will not qualify as a 1031 Exchange. This situation calls for a reverse exchange. In the typical reverse exchange, the EA forms an Exchange Accommodation Titleholder (EAT) who buys and holds (parks) the new property for you until you have closed the sale of your old property. You provide the EAT with the funds necessary to purchase the property. You are also responsible for all closing costs on the purchase, but you do not actually take title to the new property, the EAT does. Your loan to the EAT is documented by a promissory note from the EAT to you, a mortgage or deed of trust tying the money to the property. When your old property sells, the exchange proceeds go to your EA. The EAT then transfers the property to you and you use your exchange proceeds to buy the new property from the EAT. This completes your 1031 Reverse Exchange. When undertaking a reverse exchange, be careful in the selection of your lender. FHA and Fannie Mae type lenders can be a problem, because they are being asked to lend money to you, but you will not appear on a title for a short period of time. You should seek out a bank or other portfolio lender who will make a bridge loan to you which can be converted to a long-term financing when the EAT ultimately transfers the property.

### Improvement Exchanges

An improvement exchange allows you to buy a fixer-upper with part of the exchange proceeds and use the rest of the proceeds to make improvements. In an improvement exchange, when you identify the property on the 45-day list, you must also specifically say what improvements you are going to make, and how much they will cost. Like reverse exchanges, the EAT will take title to the property while the improvements are being done. You must identify sufficient improvements to use all your exchange proceeds and complete the work within the 180-day period.

### Construction Exchanges

In a construction exchange, you buy bare land with the exchange money and build a new building on the land. The EAT must buy the land for you and begin construction, but unlike an improvement exchange, you can close out your exchange before the building is completed. You must still complete your exchange before the 180 days are up. It is important to note, however, that you cannot take title to the land in your own name, or the exchange will be invalid. This is because you would be attempting to use part of the exchange proceeds for just the land, and the remainder for just the improvements and not for a completed improved property.

### Reverse Construction Exchanges

What if you cannot get enough new construction completed within 180 days of your sale to equalize and finalize your exchange? In this case, you can do a reverse construction exchange. Here the EAT takes title to the land with money borrowed from you before you sell your old property. Construction on the new property can begin and be well underway so that the construction is almost complete or fully complete when the old property closes.

### Reverse Exchange Recent Developments

The IRS issued Rev. Proc. 2000-37 (effective September 15, 2000), that provides a “safe harbor” in regard to reverse exchanges. One of the significant points in the ruling applies to time limits to reverse exchanges that are similar to those that had previously only been applied to straight exchanges.

Provisions that must be met in order to fall within the safe harbor are:

1. From the date of closing on the new property you have 45 days to determine and list the properties you want to sell;
2. Also from the date of closing on the new property you have 180 days to complete the entire reverse exchange.

### Tenancy in Common Interests in Exchanges

In March, 2002, the IRS issued Rev. Proc. 2002-22 that provides a procedural safe harbor for those who wish to acquire a fractional interest in a Replacement Property as a tenant-in-common with other people who also hold such fractional interests.

The adoption of this Revenue Procedure has resulted in an explosion of exchanges into "TIC" projects, and the birth of a whole new industry, the Tenant-in-Common industry, as exemplified by the formation of the Tenant In Common Association (TICA).

If you have thoughts about possibly investing in a fractional interest in one of these projects, call Olympic Exchange Accommodators, LLC to give you some advice on what to look for in exchanging into a TIC project.

### Vacation Homes

Vacation homes may qualify under Section 1031. Ask us for more details.

## **OVERVIEW**

### Final Remark

There are literally thousands of variations on the scenarios mentioned in this writing. At Olympic Exchange Accommodators, LLC we are glad to consult with you at any time without charge and answer your questions about any aspect of 1031 exchanges. Our exchange specialists offer you the protection and insurance you need to complete an exchange.

For the Olympic Exchange Accommodators office nearest you call: **253-512-1031**

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## **Receipt of Exchange Proceeds by Taxpayer**

Taxpayers are required under the 1991 Treasury Regulations to sign a written Exchange Agreement with a Qualified Intermediary that limits the Taxpayer's right, during the Exchange Period, to receive, pledge, or otherwise obtain the benefits of the Exchange Proceeds that come to the Qualified Intermediary from the closing of the Replacement Property.

The Exchange Period is defined as the end of the 45-day identification period if there is no identification of Replacement Properties made by the Taxpayer, and the end of the 180 day exchange period if identification has been made by the 45th day, and properties remain to be acquired after the 45th day has passed.

### **Examples**

1. Taxpayer enters into an Exchange Agreement with a Qualified Intermediary. The Relinquished Property closes with the Qualified Intermediary receiving the Exchange Proceeds from escrow. The next day after closing, Taxpayer changes his mind and decides not to complete the exchange. Taxpayer requests Qualified Intermediary to disburse the Exchange Proceeds to Taxpayer.

Qualified Intermediary cannot disburse the Exchange Proceeds until day 46, if Taxpayer does not identify any potential Replacement Properties. To do so, even though Taxpayer does not want to complete an exchange, means that the Qualified Intermediary does not abide by the restrictions of the Treasury Regulations, that the Exchange Agreement could be deemed by the Internal Revenue Service, in the event of audit, as a sham document, and imperil all other exchanges for Taxpayers assisted by the Qualified Intermediary.

2. Taxpayer enters into an Exchange Agreement with a Qualified Intermediary. The Relinquished Property closes with the Qualified Intermediary receiving the Exchange Proceeds from escrow. Taxpayer identifies two potential Replacement Properties. Taxpayer acquires one Property on day 46, but does not use all of the Exchange Proceeds. Taxpayer asks Qualified Intermediary to disburse to Taxpayer the balance of the Exchange Proceeds, as Taxpayer does not intend to acquire the other property on Taxpayer's Identification Statement.

Qualified Intermediary cannot disburse the balance of the Exchange Proceeds until day 181. Taxpayer still has one more property identified on his list. He cannot amend the Identification Statement, as the 45th day has passed. The Exchange Period continues until day 180. Qualified Intermediary must hold the Exchange Proceeds until the expiration of the Exchange Period, despite Taxpayer's protestation.



## 1031 EXCHANGES INVOLVING RELATED PARTIES

If a taxpayer exchanges property with a related person and defers the recognition of gain under Section 1031, no gain is recognized if *each* related party holds its replacement property for two years. Gain will be recognized if the taxpayer disposes of the replacement property or the related person disposes of the taxpayer's property within two years after the date of the last transfer that is part of the exchange transaction.

Rev. Rul. 2002-83: Taxpayer may not transfer relinquished property to an unrelated party and acquire replacement property from a related party if the related party has a high basis in the replacement property and receives cash or non-like kind property, pursuant to Section 1031(f).

Section 1031(f) is designed to prevent taxpayers from using Section 1031 to shift tax basis between properties owned by related parties.

The issue arises whenever a taxpayer transfers the relinquished property to an unrelated party and acquires the replacement property from a related party, even if the taxpayer holds the replacement property for more than two years.

Any person bearing a relationship to the taxpayer described in IRC § 267(b) or § 707(g)(1) is a related party, including:

- a. Members of a family (which include brothers and sisters, spouse, ancestors, and lineal descendants).
- b. Two corporations, which are members of the same controlled group.
- c. An individual in a corporation more than 50 % in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual (attribution rules apply).
- d. A corporation and a partnership if the same persons own more than 50% of the outstanding stock of the corporation and more than 50 percent of the capital interests or the profits interest in the partnership (attribution rules apply).
- e. A grantor or fiduciary of any trust.
- f. A partnership and a person owning, directly or indirectly, more than 50 percent of the capital or profits interest in such partnership (attribution rules apply).
- g. Two partnerships in which the same persons own, directly or indirectly, more than 50% of the capital or profits interest (attribution rates apply).
- h. Executor and beneficiaries of an estate.

**Call Olympic Exchange Accommodators, LLC Toll free at 1-866-309-1031**