

# → 1031 Exchange FOCUS

## Dealing with Seller Financing in a 1031 Exchange

*Internal Revenue Code Section 1031 allows investors to defer the payment of capital gains taxes when selling an investment property and exchanging into another like-kind investment property.*

---

Investors who decide to carry a note on the sale of their investment property have a few options if they are also doing a 1031 Exchange.

1. Do not include the note in the exchange. If the note is not included in the exchange, taxes will be payable using the installment method of accounting.
2. Include the note in the exchange and defer taxes owed.

With option #2, investors have several alternatives for attempting to use the note as part of the exchange. It is important that Asset Exchange Company be named as the beneficiary of the note in order to avoid any constructive receipt issues. The alternatives available to investors include:

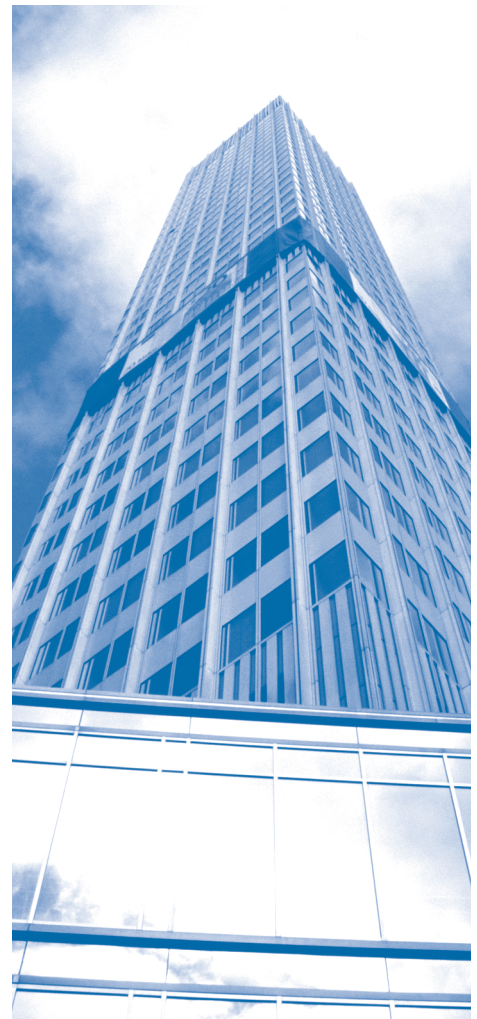
**Use The Note as Consideration for the Replacement Property:** Once the replacement property is found, the exchanger may offer the note

to the seller as payment towards the purchase price. In this case, the note is assigned to the seller by Asset Exchange Company and delivered to the seller at closing.

**Replace the Note with Cash:** In this scenario, the investor will deposit cash equal to the face value of the note into the exchange account. Asset Exchange Company will then assign the note to the exchanger for delivery at closing of the replacement property. Please note: if the note is for \$100,000—the investor must place \$100,000 cash into the exchange account.

**Sell the Note on the Secondary Market:** If the investor does not come up with cash, another option is to sell the note on the secondary market. The cash proceeds from the sale of the note are added to the exchange account. If the note is discounted, the discounted amount *may* have additional cash consequences.

SECTION 1031 OF THE INTERNAL REVENUE CODE IS ONE OF THE GREATEST WEALTH BUILDING TOOLS AVAILABLE TO THE INVESTOR



**The Note is Paid off Prior to Close:**

If the note is a short term note, it can be paid off prior to closing on the replacement property. The payer will pay Asset Exchange Company directly as the holder of the note. The paid amount is then added directly to the exchange account.

---

*The subject matter in this newsletter is intended as general information only and not intended as tax or legal advice. Please always consult your tax or legal advisor for any specific tax or legal matters.*

---

Phone: (877) 471-1031  
Fax: (877) 480-1031

info@ax1031.com  
www.ax1031.com

 **Asset Exchange Company**