

1031 Exchange

1031 Exchange: Step By Step

Internal Revenue Code Section 1031 allows deferral of capital gains taxes on real property used in trade or business or held for investment

Investors unfamiliar with 1031 Exchanges may envision the process as being intimidating and difficult. In reality, it doesn't have to be. In order to successfully complete an exchange, investors must simply follow the following basic steps.

1. Set up an Exchange Account

The 1031 Exchange account **MUST** be opened before the close of escrow on the property being sold. Waiting until the very last minute is not recommended, but Asset Exchange Company (AEC) can open a 'rush' account if necessary. AEC will need a copy of the sale contract and the contact info. for the escrow officer to open the account.

2. Add 1031 Exchange Language

The appropriate 1031 language should be added to the sale contract reflecting the sellers intent to exchange. The agent will usually add this language but AEC can provide a sample of such language if necessary.

3. Review and Execute the Exchange Agreement

The exchange agreement will be sent out for review prior to closing. Execution of the exchange documents will take place at the closing table when all other closing documents are signed.

4. Locate Replacement Property

The IRS requires that potential replacement property be identified on or before day 45 of the exchange and replacement property must be acquired on or before day 180 of the exchange.

5. Submit 45 Day Identification Letter

The identification letter **MUST** be submitted no later than day 45 of the exchange. All potential replacement properties must be identified in writing in an unambiguous manner.

6. Provide AEC with the Contract

Once in contract on replacement property, AEC will need to prepare the "Phase 2" 1031 Exchange documents. To do so, we will need a copy of the contract and the contact information for the escrow officer.

7. Request Funds for Deposits

Money for the initial earnest money deposit can be made out of pocket or disbursed from the exchange account. If personal funds are used for the deposit, clients can be reimbursed thru escrow at the closing of the replacement property.

8. Execute Phase 2 Exchange Agreement

AEC will work with the replacement property escrow company to obtain all appropriate signatures for all exchange documentation. Depending on the nature of the transaction, additional steps may need to take place. Asset Exchange Company will work closely with the client to ensure a smooth and successful transaction.

9. Report the Exchange

Reporting the exchange will be done using Federal Form 8824 for the year your Relinquished Property sold. There is no equivalent state form, so preparing Form 8824 will be sufficient to report your exchange for both your State and Federal returns. The information you provide on Form 8824 will flow to your Federal Schedule D and the equivalent State form.

Contact Asset Exchange Company

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