

# 1031 Exchange

# FOCUS

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



## > Related Party Issues in a 1031 Exchange

*Internal Revenue Code Section 1031 allows investors to defer the payment of capital gains taxes when selling investment property.*

Plan on using extreme caution when conducting a 1031 Exchange involving related parties. For such exchanges Asset Exchange Company strongly suggests discussing the plan with a tax advisor. The comments made below are a courtesy and should not be considered tax or legal advice.

### Who is a Related Party

A related party is generally a direct lineal relative such as brother, father, grandmother, daughter. Also, an entity that you or your relatives own a controlling interest in will be considered a related party. Related parties do not include stepparents, uncles, aunts, in-laws, cousins, nephews, nieces and ex-spouses.

### Sale to Related Party

When selling relinquished property to a related party, the related party buyer should plan to hold the property for at least two years prior to selling or otherwise disposing. If the related party sells the property within two years, it will create some risk to the 1031 exchange.

### Purchase from Related Party

We do not recommend buying replacement property from a related party as there is enhanced risk that the 1031 Exchange will be disallowed. The following circumstances may prove exceptions:

- If the related party sells an investment property and completes a full 1031 Exchange on their own. Both parties will then need to also hold the properties for at least two years.
- The related parties each own partial interests in multiple properties and structure a 1031 Exchange so that each party ends up owning 100% of one of the properties.
- The disposition was after the death of either of the related parties
- The disposition was an involuntary conversion, and the threat of conversion occurred after the exchange.
- You can establish to the satisfaction of the IRS that neither the exchange nor the disposition had tax avoidance as one of its principal purposes. An example of this could be if the related party sale transaction results in a larger capital gain tax than the amount deferred.

Be advised that IRS form 8824, which is used to report a 1031 Exchange, specifically asks for related party exchange information.

**Phone:** (877) 471-1031    info@ax1031.com

**Fax:** (877) 480-1031    www.ax1031.com