



© IPE 1031

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What is 1031?

Real estate and property owners who hold property for investment or for productive use in a trade or business are eligible for tax deferral of capital gains taxes as authorized by Section 1031 of the Internal Revenue Code (I.R.C.). Section 1031 should not be confused with the personal residence capital gains tax exemption provisions of I.R.C. Section 121.

By utilizing Section 1031, a qualifying taxpayer who sells property may reinvest the full proceeds of the sale, including amounts ordinarily paid as capital gains tax, into one or more "like-kind" properties. "Like-kind" property is property that is similar in nature or character. Examples of like-kind property include: rental properties, farms and ranches, offices, motels and hotels, golf courses, raw land, retail properties, industrial properties and properties leased for 30 years or more.

Most tax-deferred exchanges are classified as delayed exchanges. A basic delayed exchange occurs when a taxpayer sells "relinquished" property and exchanges it for "replacement" property within a 180-day time period. The taxpayer must adhere to other specific procedures and time period limitations.

To accomplish a successful tax-deferred exchange, taxpayers must specifically structure their transaction so that it falls within an IRS safe harbor. The safest and most common safe harbor method for structuring a tax-deferred exchange is for an exchanging taxpayer to utilize the services of a qualified intermediary, such as IPE 1031. Careful attention must be paid by the exchanging taxpayer to ensure that a qualified intermediary has been retained prior to the sale of the original relinquished property, and to ensure that the taxpayer or the taxpayer's agents do not receive any of the proceeds from the sale.

Certain persons are disqualified by Section 1031 from serving in the capacity of a qualified intermediary. Disqualified parties include a taxpaying exchanger's employee, attorney, accountant, investment banker/broker or real estate agent/broker. This restriction applies if the taxpayer's agent has served in such a capacity within the two years prior to the exchange transaction. Disqualified parties additionally include certain family members such as parents, siblings, spouses, and children; and certain business entities owned by the taxpayer. This is not an exhaustive list of persons who may be disqualified.

By utilizing Section 1031, a taxpayer can defer payment of capital gains taxes each time an exchange is done until an exchanged property is sold and cash proceeds are received.