

THE DELAYED EXCHANGE

The most common variation of tax-deferred exchange under Section 1031 is the Delayed Exchange (also known as a deferred exchange or forward exchange or generically as a tax deferred exchange). In the Delayed Exchange, the Exchangor transfers its rights under the contract of sale for the Relinquished Property to the Qualified Intermediary (QI). At the closing, the Relinquished Property is directly deeded from the Exchangor to the Buyer. The proceeds from the sale of the Relinquished Property are held by the QI until the closing of title on the Replacement Property. The Exchangor identifies one or more Replacement Properties within 45 days and closes title up to 180 days from the closing on the Relinquished Property. At the closing on the Replacement Property, the seller deeds the property directly to the Exchangor.

The steps in the process are set forth in greater detail under "The Exchange Process" section of this pamphlet.

Exchange Timetables

There are two main deadlines that the Exchangor must comply with to complete a successful exchange. Except under exceptional circumstances, the following timelines cannot be extended, even if the expiration dates fall on a weekend or legal holiday:

- ❖ The Exchange Period begins on the date on which the Exchangor transfers the Relinquished Property and ends on the earlier of the 180th day after that date or the due date (including extensions) of the Exchangor's income tax return for the taxable year in which the Relinquished Property is transferred.
- ❖ The Identification Period begins on the date the Exchangor transfers the Relinquished Property and ends at midnight on the 45th day thereafter. Identification of all Replacement Property must be made in writing and delivered to the QI or other permitted party on or before the 45th day of the close of the Relinquished Property.

Identification Guidelines

The Exchangor must notify an a permitted party in writing of the identification of the Replacement Property by midnight of the 45th day

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following the day the Relinquished Property is transferred.

There are three Identification Rules under the Regulations to choose between to identify your Replacement Property:

1. The Three-Property Rule: The Exchangor may identify up to three potential properties without regard to the fair market value of the properties identified.
2. The 200% Rule: The Exchangor may identify any number of properties as long as their aggregate fair market value does not exceed 200% of the aggregate fair market value of all the Relinquished Property”.
3. The 95% Rule: The Exchangor may identify any number of properties without regard to their value, provided, within 180 days from the date of the transfer of the first of the Relinquished Property, the Exchangor purchase properties whose value totals at least 95% of the value of all Relinquished Property.

Disaster Relief Extensions for Exchange Deadlines

The applicable regulations provide for the extension of the last day of the 45-day identification period and 180-day exchange period which falls on or after the date of a Presidentially declared disaster, by 120 days or to the last day of the general disaster extension period authorized by an IRS News Release or other guidance announcing tax relief for 1031 exchange deadlines.

Such extensions apply to victims of the specific Presidentially declared disasters. The extension is not limited, however, to an Exchangor or property being located in the area affected by the announcement, and the criteria that qualify for an extension can extend to a party or participant ancillary to the exchange being affected by the disaster. If an Exchangor believes they, or the exchange, are somehow affected by the disaster they should consult with their tax professional in conjunction with AA1031 to explore the applicability of such extension to an exchange.

Safe Harbors

The IRS regulations provide taxpayers with four safe harbors based on commonly used security, guarantee, and intermediary arrangements. The first safe harbor permits certain security arrangements. The second permits

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the use of a qualified escrow account or a qualified trust. The third permits the use of a Qualified Intermediary (QI) and the fourth permits the taxpayer to receive interest or a growth factor to compensate for the time value of money during the period between transfer of the Relinquished Property and receipt of the Replacement Property.

With the exception of the safe harbor permitting certain security arrangements, the safe harbors require an exchange agreement between the Exchangor and the QI to specifically limit the Exchangor's right to "receive, pledge, borrow, or otherwise obtain the benefits of the funds or interest in escrow or trust, money or other property" before the end of the 180-day exchange period.

A taxpayer may receive money or other property directly from another party to the transaction, but not from a qualified escrow account, a qualified trust, or a qualified intermediary, without affecting the application of a safe harbor.

The use of a Qualified Intermediary (QI) is the most common method used to complete a successful Delayed Exchange. A QI, as defined by the IRS, is a person who is not the taxpayer or "disqualified person" who acts to facilitate a Delayed Exchange by entering into an agreement with the Exchangor for the exchange of properties.

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