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Exposing 1031 myths

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Following are a few myths regarding Tax Deferred Exchanges and our attempt to set the record straight:

Myth #1: To do an exchange you must buy equal or greater - False! Believing this, taxpayers have overpaid for replacement property, assuming if they sell for $550k they must buy for $550k even if the replacement property is worth something less. Or, they skip the exchange altogether and pay taxes assuming they cannot do an exchange because they sold for $550k and their planned replacement property is only worth $475k. In truth, if the sale is at $550k their target is really $550k net of closing costs. If closing costs are $40k then their target is $510k. If the perfect replacement property is worth $475k they can purchase that and tax is calculated on the difference.

Myth #2: 1031 is only for commercial properties - Again, False! 1031 is for any property held for investment or for productive use in a trade or business. This certainly includes commercial properties but also extends to rentals and land held for investment. In fact, many exchanges involve residential rentals - single, multi-family & apartment buildings.

Myth #3: If selling a condo you must buy a condo to exchange - Yet again, False! Perhaps the second best feature of 1031 (the best being the tax deferral) is the generous definition of what qualifies as "like kind." All real estate is like kind as long as what is being sold and purchased are both held for investment or for productive use in a trade or business. The taxpayer can sell a rental and buy a commercial building - like kind! The taxpayer can sell one commercial building and buy multiple bank-owned single family rentals - like kind! The taxpayer can sell land and buy a building for their business - like kind! The combinations are truly limitless.

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