



nerej

Making offers on replacement property before a relinquished property sale - by Lynne Bagby

September 25, 2020 - Front Section

Lynne Bagby

Many New England real estate investors consider lucrative opportunities to purchase an investment property as good deals arise or sometimes when an off-market opportunity is presented. At such time, they may have a sale of an existing relinquished investment property in place (or ready to be marketed soon) that they intend to put in a 1031 exchange –yet, if the relinquished property has not closed, can they proceed with the purchase of an attractive replacement property?

In a 1031 delayed exchange, the investor has 45 calendar days from closing on the sale of a relinquished property to identify replacement properties, pursuant to the rules of identification. This 45-day period is referred to as the “Identification Period.” Some frequently asked questions are: “Can the investor begin looking for suitable replacement property before closing the sale of the relinquished property?” and “Can the investor make offers on and get replacement property under contract before closing the sale of the relinquished property?” The answers to these questions are “yes.”

Although the start of the identification period is triggered by the relinquished property sale closing, nothing prohibits an investor from looking for replacement property before the relinquished property sale closes. In fact, in many situations, this may be a very wise approach. In areas where inventory is limited and/or properties sell quickly due to market conditions, it can be a wise strategy to begin looking for replacement property once the relinquished property is under contract with a qualified buyer, or even before. The additional time before the relinquished property sale closes provides the investor more time to locate suitable replacement property. Making an offer on a replacement property before the relinquished property sale closes can be proactive and remove much of the uncertainty from the delayed exchange process. The investor should make sure to close the sale of the relinquished property before it must close the acquisition of the replacement property to avoid the need for a reverse 1031 exchange arrangement (see below for more information).

The delayed exchange timeline allows the investor 180 calendar days from the date of the relinquished property sale closing to close on the acquisition of identified replacement properties,

many investors get replacement property under contract before the relinquished property closes. In this scenario, these replacement properties can be formally identified after closing on the relinquished property sale. If the investor closes on the acquisition of any replacement properties within the 45-day Identification Period, those properties are considered identified for 1031 exchange purposes. In the event an investor locates a desirable replacement property and wants to close on that acquisition before the relinquished property sale closes, a reverse 1031 exchange is possible. There are additional costs and complexities involved with reverse exchanges, so this type of exchange makes sense on larger purchases when the higher reverse 1031 exchange fees are more than offset by the value of the replacement property acquisition.

The investor can use their personal funds for an earnest money deposit on the replacement property. The Qualified Intermediary can replace an investor's replacement property deposit with exchange proceeds for reimbursement of the investor's personal funds advanced for the replacement property earnest money deposit at the closing for the purchase of the replacement property. Investors should have their CPA review their settlement statements to be sure that the reimbursement of personal funds used for the earnest money deposit is properly reflected as well as other exchange expenses being shown properly.

Lynne Bagby, CES is the New England division manager for Asset Preservation, Inc., Boston.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540