



WHAT IS A 1031 TAX DEFERRED REAL ESTATE EXCHANGE?

A 1031 tax deferred exchange is an investment tool utilized by a property owner to save thousands of dollars in capital gain taxes. A 1031 exchange is simply the sale of property and the subsequent acquisition of a like-kind replacement property within the proper time frames. Although a 1031 exchange of property looks akin to a regular sale and purchase of property, in reality an exchange is quite different because the entire transaction is documented and facilitated as an exchange and not a sale. It is this distinction that is the difference between paying capital gain taxes on a sale and purchase of property and deferring capital gain taxes with a 1031 exchange.

By engaging in a 1031, a taxpayer is able to sell his or her property and purchase other property without losing equity to Uncle Sam in the form of taxes. For example, if an investor sold property with a gain of \$100,000, the potential tax liability can be as high as \$35,000 based on federal capital gain rates, state capital gain rates (if applicable) and depreciation recapture (if applicable). After paying capital gain taxes the investor only has \$65,000 to reinvest, where as, if the investor engages in a 1031 exchange the investor has the full \$100,000 to reinvest.

Every dollar saved in taxes allows the investor to purchase 4 to 5 times as much real estate. This is accomplished through the use of leverage. Using the above example, the investor who does not engage in a 1031 exchange uses his \$65,000 as a 20% down payment on property. With \$65,000 as a 20% down payment the investor is able to purchase a \$325,000 property. On the other hand, the investor who engages in a 1031 exchange has the full \$100,000 to use as a 20% down payment. With \$100,000 as a 20% down payment the investor is able to purchase a \$500,000 property. The investor who engaged in a 1031 exchange has \$175,000 more property than the investor who just sold property.

With proper planning one can defer capital gain taxes on rental property, vacant land, vacation properties, commercial property, agricultural land, lake shore and residential income properties.

Call Stacy Johnson, of Heartland Exchange, LLC to find out if a 1031 exchange is right for you.

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