

Structured Sale Application: 1031 Exchange “Fallback”

What if I can't find a suitable property or complete my 1031 exchange within the exchange period?

- Occasionally, a 1031 exchange cannot be completed during the allotted exchange period. Either a suitable like-kind property cannot be identified, or serious problems are identified with the property during an inspection, or financing falls through. In any event, the funds held by the qualified intermediary are released to the seller and all applicable taxes are due in the year of the sale. This can create a financial burden for the seller, one which he was trying to avoid in the first place.
- By simply adding language to the sales and 1031 exchange agreements, the seller can retain their ability to defer applicable taxes on the sale. Provisions are added to the agreements that in the event a 1031 exchange cannot be executed, a structured sale is triggered.

What if the 1031 exchange fails?

- Approximately 20% of all 1031 exchanges cannot be executed, leaving the seller to pay a sizeable, one-time tax bill in the year of sale.
- With careful and timely planning, there is a “fallback” contingency approach using a structured sale, a variation of an installment sale. The seller can preserve the ability to defer taxes on the sale and control the timing and amount of the payout of the proceeds in the event of a failed 1031.

Can I defer the taxes on the “Boot”?

- Yes. If a seller executes a 1031 exchange for a property of lesser value, we can use the Structured Sale process to defer taxes on the remaining proceeds or “Boot”. The seller can create an immediate stream of income over a set period of time. They can also defer recognition of the “Boot” for up to 20 years and receive payments at that time. Payment streams can be designed in any way the seller wishes. Taxes are deferred until payments are received and paid in the year they are received. All future payments are backed by U.S. Treasuries.

How is it done?

- The qualified intermediary is directed to send the funds to an Assignment Company which will then disperse the funds to the seller over a predetermined period of time. This stream of payments can be designed in any way the seller wants. The result is that although the 1031 exchange could not be executed, the seller can still defer the taxes over the next 3, 5 or 10 years or any period he chooses. The seller can even defer any recognition of the proceeds for up to 20 years, and then provide a guaranteed stream of income over a period of time!

Benefits and Applications

The Structured Sale has several applications when selling a highly appreciated asset such as a business or property and offers benefits to both the buyer and seller. Some of these benefits and applications include:

Benefits:

- 1) Security
 - a) All payments are guaranteed
 - b) No risk of buyer default
- 2) Flexibility of Payments / Process
 - a) Payments can be designed to meet seller's future needs
 - i) Cost of living increases
 - ii) Monthly, Quarterly, Semi-annual, Annual payments
 - iii) Multiple streams
 - b) Process – the buyer and seller can have separate cash flows.
 - i) They do not have to negotiate terms. (Seller can receive future payments while buyer pays cash!)
 - ii) Eliminates obstacles to sale
- 3) Tax Deferral
 - (a) Possible tax reduction

Applications:

- 1) Sale of a business or property
 - a) Exit strategy
- 2) Partial 1031 exchange
 - a) Structure The “Boot”
- 3) 1031 exchange “Fallback”
 - a) Tax deferral if exchange fails