Improvement Exchanges

Build New or Improve an Existing Property

1031 Knowledge

The improvement exchange allows a taxpayer, through the use of an Exchange Accommodation Titleholder (EAT) owned by a qualified intermediary, to make improvements on a replacement property using exchange equity. In other words, a taxpayer can maximize investment opportunities using tax-deferred dollars by building or improving a replacement property in a 1031 exchange. This type of exchange is also referred to as a construction or build-to-suit exchange.

Improvement exchanges offer taxpayers a wide array of benefits which often result in a better investment than properties readily available on the open market. The ability to refurbish, add capital improvements, or build from the ground up, while using tax-deferred dollars allows a taxpayer to reinvest in a replacement property that meets their precise business needs or investment criteria. Due to the additional options provided by this variation and because Revenue Procedure 2000-37 created a "safe harbor" and established parameters for improvements to be produced, improvement exchanges continue to increase in popularity.

Another benefit of the improvement exchange format is that the replacement property does not necessarily have to be fully completed within the 180-day exchange period. A certificate of occupancy is not required.

A taxpayer must meet three basic requirements in order to defer all of their gain in the improvement exchange format. The taxpayer must: 1) spend the entire exchange equity on completed improvements or down payment by the 180th day; 2) receive substantially the same property they identified by the 45th day; and 3) the replacement property must be of equal or greater value when deeded back to the taxpayer. The final value of the replacement property is the combination of the original purchase price *plus* the capital improvements made to the property. [Note: The improvements need to be in place prior to the taxpayer taking title to the replacement property if the taxpayer is seeking full tax deferral.]

The improvement exchange is commonly utilized to the benefit of taxpayers in the following situations:

- The property to be acquired in the exchange is not of equal or greater value to property being sold. In this case, the improvement exchange can eliminate a taxable situation by adding capital improvements to an existing property.
- To build a new investment from ground-up. This example maximizes the investment opportunity in a given area by enabling a taxpayer to build a replacement property that meets their exact requirements.

The main obstacle in this type of 1031 exchange occurs when there is a lender involved. This is true because throughout the improvement process, the EAT is on title to the replacement property.

<FirstName LastName>
<Title>
<Company>
<XXX.XXX.XXXX> | <XXX.XXX.XXXX>
<Email> | <Website>

ASSET PRESERVATION INCORPORATED

HQ 800.282.1031 | NY 866.394.1031
apiexchange.com | info@apiexchange.com

Asset Preservation, Inc. (API) is a qualified intermediary as defined in the regulations under Internal Revenue Code §1031. Neither API, it's officers or employees are authorized or permitted under applicable laws to provide tax or legal advice to any client or prospective client of API. The tax related information contained herein or in any other communication that you may have with a representative of API should not be construed as tax or legal advice specific to your situation and should not be relied upon in making any business, legal or tax related decision. A proper evaluation of the benefits and risks associated with a particular transaction or tax return position often requires advice from a competent tax and/or legal advisor familiar with your specific transaction, objectives and the relevant facts. We strongly urge you to involve your tax and/or legal advisor (or to seek such advice) in any significant real estate or business related transaction. © 2017 Asset Preservation, Inc. All rights reserved.