

# WHAT NOT TO DO IN A DEFERRED EXCHANGE

## "LESSONS TO BE LEARNED FROM THESE FAILED EXCHANGES"



### Compliments of

Delayed exchanges, under IRC Section 1031, are the most common exchange format nationwide. The IRS has structured exchanges with strict guidelines for full tax deferral. In a delayed exchange, a property owner must meet a number of key time deadlines after closing on the sale of a relinquished (also referred to as the sale or Phase I) property:

1. Acquire the replacement property (s) within 180 calendar days, or the day the Ex-changer's tax return is due, whichever is earlier (the "Exchange Period")
- AND -
2. Either acquire all replacement properties or properly identify all potential replacement properties within 45 calendar days (the "Identification Period").

Listed below are three recent examples of what not to do in a deferred exchange:

### **CHRISTENSEN VS. COMM. (April 10, 1998)**

*What Happened:* The Christensen's filed their tax return on April 15 and acquired replacement property within 180 days, but this purchase closed after they had already filed their tax return. The Tax Court cited failure to comply with the deadlines, specifically the requirement to complete the exchange within 180 days OR the tax filing date, whichever is earlier, as the reason tax deferral was not allowed.

*What Should Have Happened:* They should have filed an extension prior to their closing to obtain benefit of the entire 180 day exchange period.

### **KNIGHT VS. COMM. (March 16, 1998)**

*What Happened:* On day 179, the Knight's purchase of their replacement property fell apart. The Knight's acquired another property after the 180th day and argued they made a "good faith" attempt to meet the time requirements. The Tax Court denied the exchange because the tax code clearly allows only a maximum of 180 days to complete the exchange.

*What Should Have Happened:* The Knights should not have postponed their acquisition to last moment, if at all possible. Had more time been available, they may have been able to acquire another properly identified property before their 180th day.

### **DOBRICH VS. COMM. (October 20, 1997)**

*What Happened:* The Dobrich's intentionally "back-dated" an Identification Notice. This was discovered by the IRS and they were *liable for \$2.2 Million in capital gain taxes PLUS a \$1.6 Million fraud penalty!*

*What Should Have Happened:* The Dobrich's should have acquired only property identified within the 45 day Identification Period. Under no circumstances should investors ever back-date Identification Notices!



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