1031 MYTH Busters

Myth or Fact: There are many misconceptions on 1031 exchanges and we want to make sure you know the facts.

1031 exchanges directly benefit millions of American businesses and investors every year. Section 1031 encourages businesses to expand domestically and grow the U.S. economy. Industry studies show that Section 1031 is vitally important to creating new transactional activity domestically, encouraging small businesses to expand, fostering job creation and contributing to economic growth nationwide. Investors and businesses in many industries, including residential and commercial real estate, transportation, equipment/vehicle rental/ leasing, and construction rely on 1031 exchanges to grow their businesses.

MYTH:

I do not own real estate so a repeal of section 1031 will not affect me.

FACTS:

Everyday, American consumers benefit from 1031 exchanges. Here are just a few examples:

1. **Purchasing Products or Services**: Americans pay less for products and services because businesses can use 1031 exchanges to replace equipment rather than using capital which helps keep costs lower. The products are then delivered by a company that probably exchanges its delivery fleets keeping their costs down (and keeps the fleets turned over regularly ensuring the vehicles on the road are better maintained). Farmers regularly use section 1031 to acquire better farmland and replace farm equipment and livestock.

2. **Renting a Place to Live**: Exchangers make up a large percentage of owners of single family home rentals and multi-family rental properties. The ability to exchange allows the exchanger to reinvest all net proceeds into the replacement property which requires less financing. This helps keep the cost of ownership down and allows the property owners to rent for less.

3. **Using Public Transportation**: Most public transportation fleets (buses, trains and taxis) are regularly exchanged for replacement vehicles, keeping the cost of ownership down so that the cost for users stays down.

4. **Traveling this Holiday Season**: Airlines often use 1031 exchange to update their fleet and rental cars are the most frequently exchanged assets. Again, the ability to exchange helps keep costs down for consumers.

MYTH:

1031 is for big real estate investors.

FACT:

60% of real property exchanges involve the sale of properties less than $500,000 and 50% involve the sale of properties less than $1,000,000. Almost 2/3 of all exchanges facilitated by 1031 CORP. involve the sale of a single-family home.

MYTH:

Tax on deferred gain is never paid.

FACT:

The 2015 Ling Petrova Study found nearly 88% of exchanged commercial real estate replacement properties are eventually disposed of in a taxable sale resulting in substantially more tax being paid than would have been due had the exchange not occurred.

MYTH:

Real estate developers use 1031 to get rich.

FACT:

Section 1031 prohibits real estate developers, builders and “flippers” from using exchanges when they sell property. Section 1031 would only be beneficial to someone who builds a business use or investment property and holds it. Not only do these builders, developers and “flippers” not benefit from section 1031 when they sell but they are taxed at much higher ordinary income tax rates than lower capital gains.

MYTH:

The economy has rebounded so section 1031 is no longer an essential strategy for growth.

FACT:

The Tax Foundation found a repeal of section 1031 would reduce the annual GDP by $18 Billion and cost the U.S. 23,000 full-time jobs. There would also be a “lock in” effect on real estate because investors and business owners will not want to sell their property due of the potential tax liability. All of these factors could, unfortunately, create another recession.

For more information on threats facing §1031 or to help preserve §1031, visit www.1031taxreform.com

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