



Utilizing a DST in a 1031 Tax-Deferred Exchange

1031 | DST

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> Defer Capital Gains Tax

Section 1031 of the Internal Revenue Code provides an effective strategy for deferring capital gains tax that may arise from the sale of a business or investment real property. By exchanging the real property for like-kind real estate, real property owners may defer taxes and use the proceeds to purchase replacement property. Like-kind real estate includes business and investment real property, but not the property owner's primary residence.

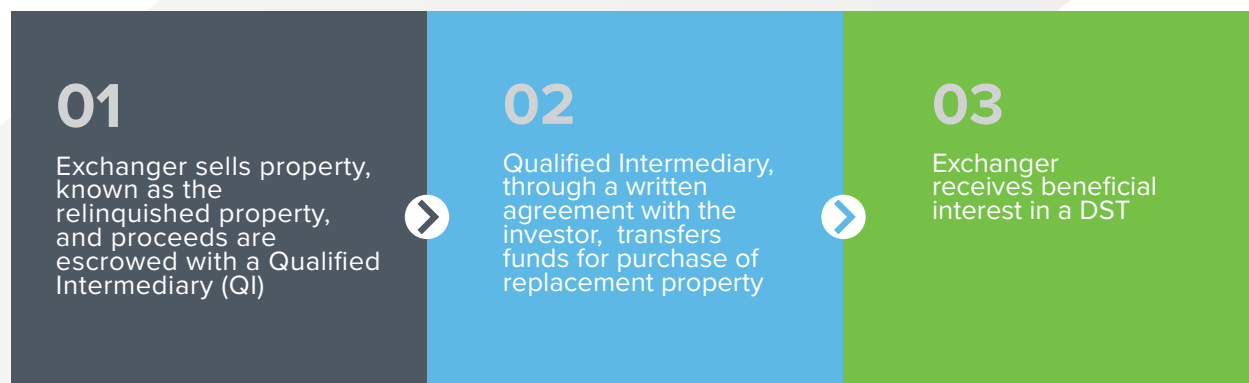
It is important to note that there are several specific guidelines that must be followed in order to successfully execute a 1031 exchange transaction. For instance, the cash invested in the replacement property must be equal to or greater than the cash received from the sale of the relinquished property. In addition, the sum of the cash invested and the debt placed on the replacement property must be equal to or greater than that of the relinquished property. In other words, additional cash can make up for a shortfall in debt placed on a replacement property, but additional debt cannot make up for a shortfall in cash invested in a replacement property. Prospective investors should consult their tax advisors regarding a 1031 exchange.

> Fractional Ownership Through DSTs

A Delaware statutory trust (DST) permits fractional ownership of real estate, in which multiple investors can share ownership in a single property or a portfolio of properties. This structure may qualify as replacement property as part of a 1031 Exchange. Also, DST investments are passive in nature where property management decisions and day to day operations are left to the trustee."

> Investors with Property to Exchange

A typical 1031 exchange involving the eventual investment into a DST has three basic steps:



The Role of a Qualified Intermediary

The QI is a company that facilitates Section 1031 tax-deferred exchanges. The QI enters into a written agreement with the investor where the QI transfers the relinquished property to the buyer, while transferring the replacement property to the investor pursuant to the exchange agreement. The QI holds the proceeds from the sale of the relinquished property in a trust or escrow account in order to ensure the investor never has actual or constructive receipt of the sale proceeds, which would trigger capital gain consequences.



> Key Benefits of DST 1031 Exchanges

NO MANAGEMENT RESPONSIBILITIES

The DST is the single owner and agile decision maker on behalf of investors.

ACCESS TO INSTITUTIONAL-SIZE PROPERTY

Most real estate investors cannot afford to own multi-million dollar properties. DSTs allow investors to acquire partial ownership in properties that otherwise would be out-of-reach.

LIMITED PERSONAL LIABILITY

Loans are nonrecourse to the investor. The DST is the sole borrower.

DIVERSIFICATION

Investors can divide their investment among multiple DSTs, which may provide for a more diversified real estate portfolio across geography and property types.

ESTATE PLANNING

DST investments are eligible for a step up in cost basis so your heirs will not inherit capital gain liabilities. DSTs also save your heirs from many of the burdens of owning real estate through professional management.

INSURANCE POLICY

If for some reason the investor cannot acquire the original property they identified, a secondary DST option allows them to meet the exchange deadlines and defer the capital gains tax.

ELIMINATE BOOT

Any remaining profit on the sale of your relinquished property is considered “boot.” This remaining money becomes taxable unless you eliminate it. The excess cash (boot) can be invested in a DST to avoid incurring tax.

SWAP UNTIL YOU DROP

The DST structure allows the investor to continue to exchange real properties over and over again until the investor's death.



> 1031 Exchange Timeline



> Like-Kind Real Estate

To complete a successful Section 1031 tax-deferred exchange, the replacement property must be like-kind to the relinquished property. Some examples of like-kind properties include:

- Multifamily Apartments
- Healthcare
- Self-Storage Facilities
- Retail Centers
- Industrial Warehouses
- Student Housing
- Senior Living
- Hospitality

Any real estate held for productive use in a trade or business or for investment purposes is considered like-kind. A primary residence would not fall into this category, however, vacation homes or rental properties may qualify.

EXAMPLES OF LIKE-KIND DST PROPERTIES

- | | | | |
|------------------------|------------------------|--------------------|---|
| OFFICE BUILDINGS | SINGLE-FAMILY RENTALS | HOTELS AND MOTELS | EASEMENTS |
| RETAIL CENTERS | APARTMENT BUILDINGS | MINERAL RIGHTS | TENANCY-IN-COMMON (TIC) INTERESTS |
| WAREHOUSES | CONDOMINIUMS | WATER RIGHTS | DELAWARE STATUTORY TRUST (DST) INTERESTS |
| VACANT LAND | INDUSTRIAL PROPERTY | AIR RIGHTS | LEASEHOLD INTERESTS (30 YEARS REMAINING ON LEASE) |
| DUPLEXES AND TRIPLEXES | RENTAL RESORT PROPERTY | DEVELOPMENT RIGHTS | NEW YORK COOPERATIVES |



APARTMENT



NET LEASE RETAIL



OFFICE



SELF STORAGE



INDUSTRIAL



GOVERNMENT



MINERAL ROYALTIES



LAND



HOTEL

GLOSSARY OF COMMON TERMS

Accredited Investor: Defined in Rule 501 of Regulation D to refer to investors who are financially sophisticated and have a reduced need for the protection provided by certain government filings. While each state may have additional accreditation requirements, individuals are generally considered to be accredited if they (i) have a minimum net worth exceeding \$1,000,000 for individuals, including spouse or spousal equivalent (excluding the value of your primary residence), (ii) a minimum annual income requirement for the past two years of \$200,000 per year for an individual; or \$300,000 per year, including spouse or spousal equivalent and a reasonable expectation of the same income level in the current year, (iii) an individual who is licensed and in good standing as a (a) General Securities Representative (Series 7), (b) Licensed Investment Adviser Representative (Series 65), or (c) Licensed Private Securities Offerings Representative (Series 82), or (iv) a “knowledgeable employee” as defined under the Investment Company Act of 1940, of the Trust or the Trustee or an affiliated management person of the Trust, such as the Sponsor.

Boot: Any consideration other than “like-kind” property received by the investor. Boot is subject to taxation to the extent there is capital gain. Boot can accumulate over each exchange and is retroactive back to the original relinquished property. Boot can refer to cash boot, mortgage boot and personal property.

Cash Boot: Any funds received by the Exchanger—either actually or constructively—from the sale of the relinquished property.

Constructive Receipt: Exercising control over your exchange funds or other property including having money or property from the exchange credited to your bank account or property or funds reserved for you. Being in constructive receipt of exchange funds or property may result in the disallowance of the tax-deferred, like-kind exchange transaction thereby creating a taxable sale. An example of constructive receipt would be the investor selling his relinquished property and having a closing officer hold the proceeds in an escrow or trust account on his behalf.

Direct Deeding: Either the relinquished property or the replacement property can be deeded directly from seller to buyer without deeding the property to the Qualified Intermediary. Direct deeding may eliminate paying transfer taxes twice on the sale of the relinquished property and purchase of the replacement property.

Exchange Agreement: The written agreement defining the transfer of the relinquished property, the subsequent receipt of the replacement property and the restrictions on the exchange proceeds during the exchange period. The exchange agreement specifies all the terms of the relationship between the investor and the qualified intermediary.

Exchange Period: The period of time during which an investor must complete the acquisition of the replacement property in a like-kind exchange transaction. The exchange period is 180 calendar days from the transfer of the investor's relinquished property, or the due date (including extensions) of the investor's income tax return for the year in which the tax-deferred, like-kind exchange transaction took place (whichever is earlier), and is not extended due to holidays or weekends.

Exchanger: An individual, married couple or any other entity such as a corporation, limited liability company, partnership or trust. An investor has property and would like to exchange it for new property.

Identification Period: The period of time during which an investor must identify potential replacement properties for a tax-deferred, like-kind exchange. The period is 45 calendar days from the transfer of the investor's relinquished property and is not extended due to holidays or weekends.

Like-Kind Property: Any two assets or properties that are considered to be the same type under federal income tax law, making an exchange between them tax deferred. Like-kind real estate property is basically any real estate that is not held for personal use, including a second home which is held for investment purposes. Following the Tax Cut and Jobs Act of 2017, like-kind property is limited to real property.

Mortgage Boot: Mortgage Boot occurs when the Exchanger does not acquire debt that is equal to or greater than the debt that was paid off, and is therefore ‘relieved’ of debt, which is perceived as taking a monetary benefit out of the exchange. Therefore, the debt relief portion is taxable, unless offset by adding equivalent cash to the transaction.

Private Placement Memorandum (“PPM”): A legal document stating the objectives, risks and terms of investment involved with a private placement. This may include items such as the financial statements, management biographies, detailed description of the business, etc. A PPM serves to provide buyers with information on the offering and to protect the sponsor from the liability associated with selling unregistered securities.

Qualified Intermediary: Also called: intermediary, QI, accommodator, facilitator, or qualified escrow holder. The QI is a third party that holds exchange funds and helps to facilitate the exchange.

Regulation D Offering: An exemption from registration of securities offerings under U.S. Securities laws often used for TIC and DST ownership investments where, among other factors, investors generally must be qualified as accredited investors.

Relinquished Property: The original property given up by the investor which is sold by the qualified intermediary. This property is sometimes also referred to as the sale, “downleg” or “Phase I” property.

Replacement Property: The like-kind property to be acquired or received by the investor from qualified intermediary's purchase from the seller in a tax-deferred exchange transaction. This property is sometimes also referred to as the purchase, “upleg” or “Phase II” property.

Reverse Exchange: A reverse 1031 Exchange represents a tax deferment strategy when for a variety of reasons, the replacement property must be purchased before the relinquished or old property is sold. It is more complex than a forward 1031 Exchange and requires careful planning.

Sponsor: The party offering a commercial property asset available for sale to investors. The sponsor purchases the property, arranges the financing (if any), sells the fractionalized interests to individual investors, and typically handles accounting and property management after closing.



Our third party, 1031/DST provider helps investors navigate obstacles and fix problems which commonly occur during a 1031 Exchange by utilizing and leveraging DSTs.

For more info, or to book a consult contact:

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