



# IPX 1031

## REVERSE ORDER FORM

Please Return by Facsimile to Our Offices  
Fax: (510) 891-8664

### Initial Exchange Information

1. Client Name: \_\_\_\_\_
2. Street Address: \_\_\_\_\_
3. City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_
4. Phone (W) \_\_\_\_\_ (H) \_\_\_\_\_
5. Fax: \_\_\_\_\_
6. Social Security Number: \_\_\_\_\_
7. **Relinquished** Property Address: \_\_\_\_\_
8. Buyers Agent: \_\_\_\_\_ Phone: \_\_\_\_\_
9. Sellers Agent: \_\_\_\_\_ Phone: \_\_\_\_\_
10. Escrow Number: \_\_\_\_\_
11. Escrow Officer/Escrow Assistant: \_\_\_\_\_  
Phone: \_\_\_\_\_ Fax: \_\_\_\_\_
12. Is There Seller-Carry Back Financing? \_\_\_\_\_
13. **Replacement** Property Address: \_\_\_\_\_
14. Buyers Agent: \_\_\_\_\_ Phone: \_\_\_\_\_
15. Sellers Agent: \_\_\_\_\_ Phone: \_\_\_\_\_
16. Escrow Number: \_\_\_\_\_

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Phone: 510-645-6100



17. Escrow Officer/Escrow Assistant: \_\_\_\_\_

Phone: \_\_\_\_\_ Fax: \_\_\_\_\_

18. Is There Seller-Carry Back Financing? \_\_\_\_\_

19. Tax Advisor: \_\_\_\_\_

Phone: \_\_\_\_\_ Fax: \_\_\_\_\_

<b>Relinquished Property</b>	
<small>(only show numbers for Exchanger's ownership interest)</small>	
<b>FMV:</b>	_____
<b>Debt:</b>	_____
<b>Equity:</b>	_____

<b>Replacement Property</b>	
<small>(only show numbers for Exchanger's ownership interest)</small>	
<b>FMV:</b>	_____
<b>Debt:</b>	_____
<b>Equity:</b>	_____

Carry-Back Note: \_\_\_ No \_\_\_ Yes, Amount: \$ \_\_\_\_\_

**Initial Items Required:**

1. Purchase and Sale Agreements with Exchange Addendum or Cooperation Clause
2. Preliminary Reports on each property



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## BRIEF EXCHANGE

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### Avoiding the Reverse Exchange

Although the new IRS Revenue Procedure 2000-37 that provides "safe harbor" guidelines for reverse and improvement exchanges and has removed the tax risk associated with these types of exchanges, there are still many reasons why Exchangers may want to treat reverse exchanges as a last and final option. Reverse exchanges require the Exchanger to place a significant level of trust in their accommodation company, and reverse exchanges, when done right, are not inexpensive. Additionally, it may not always be possible to structure a reverse exchange with an accommodator who is willing or able to hold title. In addition, the properties to be held may be contaminated, or the down payment on the Replacement Property may not exceed the expected proceeds from the sale of the Relinquished Property.

In these circumstances it is important to know the options available to an Exchanger to avoid a reverse exchange. On the continuum of "least to most aggressive" the options are as follows:

1. Ask the Seller of the Replacement Property for an extension of the closing. If needed, this request can be supported with an additional earnest money deposit.
2. Reduce the asking price of the Relinquished Property to encourage a quick sale.
3. Don't use this particular property as the Replacement Property in the Exchanger's exchange. Pick another Replacement Property.
4. Buy an extension of closing from the Seller with a non-applicable, non-refundable earnest money deposit.
5. Offer to purchase an option or right of first refusal to purchase the Replacement Property.

If the Exchanger is willing to tolerate some additional risk and needs to occupy the Replacement Property, he may choose to enter into a lease agreement with an option to purchase with the Seller of the Replacement Property. Exchangers should note that the IRS might interpret this as the Exchanger receiving the benefits and burdens of property ownership even though they do not have legal title, which could cause problems for the exchange.

In the past, if none of the above options eliminated the need for a reverse exchange, the Exchanger may have decided to have a friend, brother-in-law, or business associate take title to the target property to avoid the costs associated with professional accommodators. Since Rev. Proc. 2000-37 we do not recommend Exchangers attempt such "home-made" reverse exchanges. Unless a tax advisor experienced in reverse exchanges under Rev. Proc. 2000-37 who is able to draft a Qualified Exchange Accommodation Agreement to cover the transaction is guiding the Exchanger, this exchange structure might not be afforded safe harbor protection of the Revenue Procedure possibly resulting in a failed exchange.

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### Relinquished Property Parked Reverse – Structure

As with the other types of reverse or improvement exchanges facilitated by IPX1031, separate entities act as a Holding Entity and Qualified Intermediary. The relinquished property Parked Reverse Exchange structure can be divided into three phases. Although the Holding Entity will continue to be on title to the relinquished property, from a tax reporting standpoint the exchange is concluded at the end of Phase II.

#### Phase I: Holding Entity Agrees to Purchase Relinquished Property:

The Holding Entity enters into a purchase agreement with the Exchanger to acquire the relinquished property. The Exchanger must establish the sales price for this agreement. To achieve the maximum benefit for the exchange the price the Holding Entity will pay should equal the expected net sales price on the sale of the property to a true third-party buyer. The Exchanger should work with their tax advisor to determine the sales price. Exchangers should be advised not to place too low of a price on the sale of the relinquished property, as it could pose the potential of creating boot in the form of excess cash sales proceeds when the property is eventually sold to the true buyer and the Holding Entity's loans are repaid.

The Exchanger must also arrange for financing for the Holding Entity to acquire the property. Financing may take one or more of the following forms: (1) cash loan from the Exchanger, (2) new loan from a third-party, (3) assumption of the existing loan by the Holding Entity, (4) the Holding Entity taking the property "subject to" the existing loan, or (5) carry-back loan from Exchanger. If the Holding Entity is obtaining new financing or assuming the existing debt, the loan documents must state that the Holding Entity will have no personal liability and that the loan is non-recourse to the Holding Entity. If the financing is a carry-back loan from the Exchanger, the general rules on exchanging with seller carry-back notes are applicable, and the carry-back note must be converted into cash to be used to acquire the replacement property.

If a closing file for the relinquished property has not previously been established with a settlement agent, a file will need to be opened with the settlement agent of the Exchanger's choice, or with the local Fidelity National Title or Chicago Title office if the client does not express a preference. When possible, it is generally preferable to open this file with the same person who is handling the replacement property transfer. The Holding Entity will require title insurance. Once on title, the Holding Entity will enter into a Lease Agreement with the Exchanger or their affiliate as the tenant. The Lease Agreement will be effective as of the day of closing.

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### Relinquished Property Parked Reverse – Structure (cont.)

#### Phase II: Simultaneous Exchange:

IPX1031 will act as the Qualified Intermediary by acquiring (through assignment) and transferring the relinquished property to the Holding Entity. IPX1031 will direct the exchange proceeds to be transferred from the relinquished property closing to the replacement property settlement agent to be used to close the replacement property.

IPX1031 will then assign into the Exchanger's rights as buyer of the replacement property and use the exchange proceeds for closing and instruct the settlement agent to deed the replacement property directly from the seller to the Exchanger.

#### Phase III: Holding Entity Sells Relinquished Property:

The Holding Entity should be the party entering into the new listing agreement with the real estate agent listing the property. The Holding Entity will then continue to hold title to the relinquished property with the Exchanger as the tenant under the Lease until the Exchanger has located a third-party buyer for the relinquished property. When a purchase agreement is satisfactory to both the Holding Entity and the Exchanger, the Holding Entity will sign the purchase agreement.

While it is not required, it is preferred that the settlement of this sale to the true buyer be handled by the same settlement agent who handled the transfer of the relinquished property to the Holding Entity. In order to transfer clear title, the Holding Entity will instruct the settlement agent to pay-off any loans not being assumed by the third-party buyer.

If the proceeds from the sale of the relinquished property paid to the Holding Entity exceed the principal and interest balance of the loans (both from the Exchanger and any third-parties) and the Exchanger has not identified any additional replacement property, the excess will be returned to the Exchanger as taxable boot. Note, however, if the Holding Entity's sale of the relinquished property occurs within forty-five days of the transfer of the relinquished property to the Holding Entity, then the exchange proceeds received by the Holding Entity that are in excess of the loan balances will be returned to IPX1031. The Exchanger can either have IPX1031 acquire additional replacement property with the excess funds, or receive them on the 46<sup>th</sup> day as boot.

If the proceeds paid to the Holding Entity are insufficient to pay the Holding Entity's debt, the funds will first be applied to pay-off any third-party loans the Holding Entity assumed, took subject to, or created. Any remaining funds will then be credited to the Exchanger, who will agree to take such funds as payment in full satisfaction of its loan to the Holding Entity.

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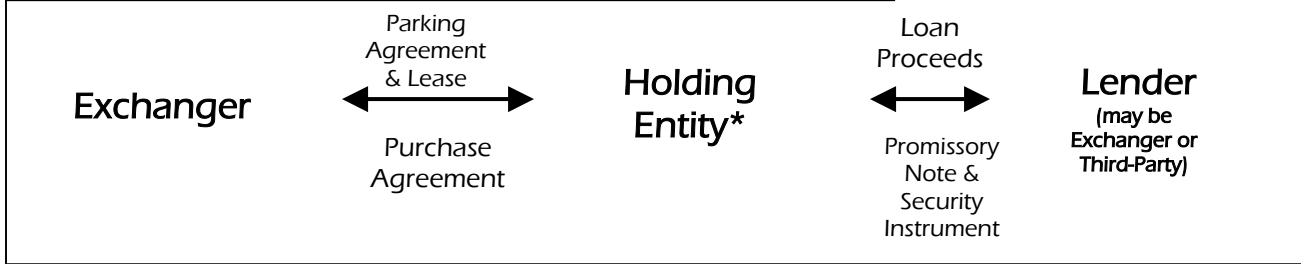
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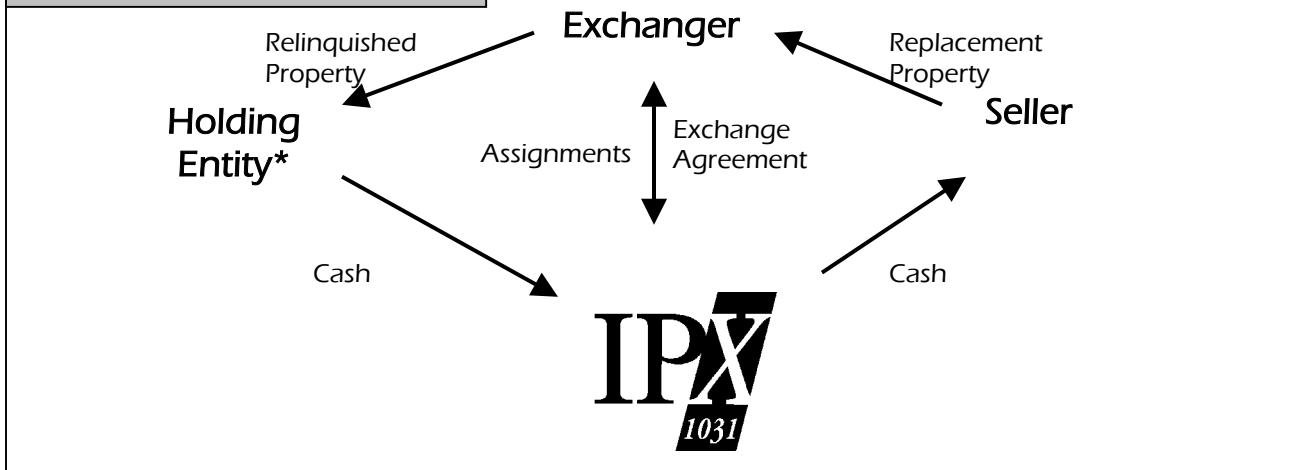
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Flow-Chart for a "Relinquished Property Parked" Reverse Exchange

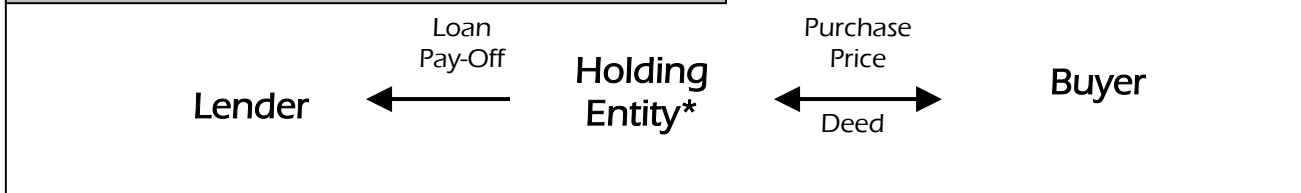
**Phase I: Holding Entity\* Agrees to Purchase Relinquished Property**



**Phase II: Simultaneous Exchange**



**Phase III: Holding Entity Sells Relinquished Property**



\* The Holding Entity is also known as the Exchange Accommodation Titleholder (the "EAT") under Revenue Procedure 2000-37



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### Insurance Requirements

Under the terms of our Lease Agreement (in reverse exchanges) or Project Management Agreement (in improvement exchanges) the responsibility of providing hazard and liability insurance coverage for a property held by IPX1031 lies with the Exchanger. Prior to taking title, IPX1031 will require proof of both liability and property coverage naming the Holding Entity as an additional named insured.

The required coverage limits will be determined by the value and the nature of the use of the parked property. Property insurance coverage will need to be for the replacement value of the parked property. The minimum liability insurance limit for IPX1031 is \$1,000,000.00, and the minimum requirements generally increase according to the following table.

Property Value	Nature of Property Use	Required Minimum Liability Coverage
Any Value	Residential (under 4 units)	\$ 1,000,000
Under \$ 1,000,000	Vacant Land	\$ 1,000,000
Under \$ 1,000,000	Commercial/Multi Housing	\$ 1,000,000
\$ 1M to \$ 5M	Vacant Land	\$ 1,000,000
\$ 1M to \$ 5M	Commercial/Multi Housing	\$ 2,000,000
Over \$ 5M	Commercial/Multi Housing	\$ 5,000,000

Owners of commercial liability insurance policies generally will not find adding the required coverage listing the Holding Entity a problem. Exchangers operating rental houses out of personal liability policies may encounter some problems meeting the \$1,000,000 minimum limit. Exchangers who do not own commercial liability insurance policies will want to confirm the available coverage limits with their agent.

Exchangers encountering problems obtaining the required minimum insurance coverage should speak with their IPX1031 Regional Office regarding possible alternatives.

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## Structuring the Reverse Exchange

### Parking the Replacement Property

In structuring a reverse exchange, our preference is generally to park title to the Replacement Property; however, it may not always be possible or desirable for us to hold title to the Replacement Property. There are three key elements we will look at to help determine if we are comfortable taking the Replacement Property.

#### 1. New Financing

If the Exchanger is getting new financing, time constraints or lender requirements may not allow us to hold title. This is a particular concern when the Replacement Property is residential in nature, as residential loans are typically sold on the secondary market. Because we require a loan to be entirely non-recourse as to the holding entity and assumable by the Exchanger, our loans are not marketable, and most residential lenders will not wish to participate.

*(See Brief Exchange on Third Party Notes and Security Instruments for the suggested loan non-recourse and assumption language)*

One way around this challenge for reverse exchanges done under the guidance of Rev. Proc. 2000-37 is to have the loan made to the Exchanger directly. The Exchanger would then simultaneously loan those funds to our Holding Entity. Our Holding Entity would give the Exchanger a Promissory Note and a Deed of Trust or Mortgage. The Exchanger would then assign those documents to the lender for collateral on its loan. While this approach will help prevent the lender from having to take a non-recourse note, it will do nothing to appease the lender who is looking for a "cookie-cutter" deal, and the Exchanger should be made aware that there will probably be higher bank fees assessed for their troubles.

#### 2. Environmental Status

Is there a clean environmental report on the Replacement Property? Unless the Replacement Property is residential (under four units) or undeveloped residential land we will require a Phase I Environmental Site Assessment Report. We may be willing to accept a Transaction Screen on raw land or vacant lots. Because our interests are different than a bank's, we may require the environmental report even though the lender is comfortable without one.

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## Structuring the Reverse Exchange (Cont.)

### 3. Nature and Use of Property

If given the opportunity we like to stay away from gas stations, corporate pig farms, dry cleaning facilities, meat packing plants, race tracks, properties under construction (if improvements are not necessary to the exchange) and any other type of facility that may expose us to environmental claims or greater than average liability. While we don't have a general policy to refuse to take title to these higher risk properties, we will definitely take the nature of the property into account when structuring and pricing the exchange.

### Parking the Relinquished Property

If one of the above conditions prevents us from holding title to the Replacement Property, or if the Exchanger has a preference for us not to hold title to the Replacement Property, we will look to the Relinquished Property. There are several considerations when determining if we can park the Relinquished Property.

#### A. Roll-Over of Equity

The largest impediment to the Relinquished Property parked exchange is the requirement that the down payment in the Replacement Property be equivalent to the equity in the Relinquished Property upon closing. To have a complete tax deferral the Exchanger's down payment on the Replacement Property must equal or exceed the expected proceeds from the sale of the Relinquished Property. If the Exchanger does not have sufficient cash for the down payment, or if the Relinquished Property sells for more than anticipated the Exchanger will have boot.

#### B. Environmental Status

As with the Replacement Property, unless the Relinquished Property is residential in nature and under four units we will require an environmental report prior to taking title. This requirement can be especially troublesome for Relinquished Property that is not currently under contract. Most commercial contracts will call for a Phase I E.S.A. as part of the due diligence, but if there is no contract the Exchanger may not have completed any environmental reports.

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## Structuring the Reverse Exchange (Cont.)

### C. Timing

Even though a Relinquished Property parked exchange may work on paper, timing may prohibit us from facilitating such an exchange. Unless the Relinquished Property is currently in escrow or the settlement agent is sufficiently motivated, it will take longer than our usual one-week set-up period. Exchangers should be aware that they might need to delay the close of the Replacement Property by a week or more to allow us to get everything in order to close the Relinquished Property side.

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