

The Home Edition

An Alternate Route

Volume 13, Issue 4

September/October 2005

A Guide to Reverse Exchanges

source: ROCHELLE STONE, JOHN MANGHAM from the August 2005 Issue of Realtor Magazine



Betty vacations at the beach each year. This year she decides to buy an investment property there. With the help of a real estate salesperson, she finds the perfect condo unit—at a below-market price of \$400,000. Betty wants to use the proceeds from the sale of her rental house, another investment property, to buy the condo. To defer taxes on the capital gain, she plans to use a 1031 tax-deferred exchange. However, because of the hot beachfront market, Betty is afraid to wait to make an offer on the condo until she's found a buyer for her property. To solve the timing problem without losing the deal, the salesperson suggests a reverse exchange.

A reverse exchange shares similar requirements with the more common deferred exchange. In a delayed exchange, once an exchanger has sold the property to be relinquished, the person must use a qualified third party (an

intermediary) to receive the sales proceeds at closing and then use the money to acquire title to the replacement property.

However, in a reverse exchange, a second intermediary, called an accommodation titleholder, takes title to either the relinquished or the replacement property since the exchanger can't hold title to both properties at once. The AT may remain as the owner for 180 days, allowing the exchanger time to locate a buyer for the property to be relinquished. Note: The two intermediaries in a reverse exchange can be the same person.

Like the more common delayed exchange, in which the property the exchanger owns is sold first, a reverse exchange allows exchangers to defer taxes completely if they use all net proceeds from the sale of a property to purchase a replacement property of equal or greater value.

There has been a significant increase in reverse exchanges since 2000, when the Internal Revenue Service issued Revenue Procedure 2000-37, which set guidelines for those transactions. In fact, some investors look for replacement properties before marketing property they intend to relinquish.

Reverse basics

Under IRS rules for reverse exchanges,

- Investors must use an AT to purchase and warehouse either the relinquished or the replacement property for up to 180 days.
- The AT can't be the exchanger undertaking the exchange or a disqualified person, as defined by the Omnibus Budget Reconciliation Act of 1989. A disqualified person is anyone who has acted as the exchanger's agent within the preceding two-year period, including an attorney, an accountant, an investment banker, or a real estate broker.
- The AT must be named on the title of either the replacement or the relinquished property.
- There must be a written qualification exchange accommodation agreement between the exchanger and the AT defining the intent and obligations of the parties and the restrictions on the proceeds by the exchanger.
- The exchange agreement must state that the AT will be treated as the beneficial owner of the warehoused property for federal tax purposes, including reporting interest and depreciation.
- The property to be exchanged must be identified in 45 days, and the transaction completed in 180 days, just as required for a delayed exchange.
- The exchanger may make and guarantee loans with the warehoused property as collateral, lease or manage the property being warehoused, or supervise construction or act as the contractor for improvements on the warehoused property before the exchange is final.

Structuring reverse exchanges

A reverse exchanger must have liquid financial resources to make the exchange viable. Reverse exchanges can be structured in two ways, depending on the exchanger's resources and the financing available.

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An Alternate Route by Rochelle Stone, John Mangham (continued from page 1)

Option 1. The exchanger has sufficient funds to purchase the replacement property for cash, or the seller of the replacement property will take back financing. Under this option, the exchanger “lends” the AT the money to buy the replacement property. Once a buyer purchases the relinquished property, the intermediary uses the proceeds from the sale to acquire the replacement property from the AT and deed it back to the exchanger.

Option 2. When the exchanger doesn’t have the funds to purchase the new property for cash, the transaction must be structured differently. In this case, the exchanger must obtain cash from a line of credit or other source and then “lend” those funds to the AT so that the AT can purchase the relinquished property. The sale to the AT means there are proceeds the intermediary can use to purchase the replacement property.

The intermediary then deeds the replacement property to the exchanger, who can now use the property as collateral for the new mortgage loan. The subsequent sale of the relinquished property by the AT provides the funds to pay back the exchanger’s loan to the AT.

Although reverse exchanges are complicated and require financial strength, real estate practitioners and their investor clients would be well served to add this powerful financial tool to their portfolio.

Stone is the president and founder, and Mangham, CPA, is the southwest regional manager of Starker Services Inc., a national company that performs all types of 1031 tax-deferred exchanges. You can reach the authors at rstone@starker.com or 800/332-1031



A Consumer’s Guide to Carpet Cleaning

brought to you by Conscientious Carpet Care

Which Method Cleans Best?



Dry Foam

The carpet cleaner applies shampoo to your carpet, allows it to dry, then, without rinsing, sucks the dried shampoo into a vacuum. Can you imagine applying shampoo to your hair, allowing it to dry then removing the shampoo from your head with a vacuum? This method leaves dirty residue in your carpet, which is one reason why dry foam is not very effective.

Absorbent Pad (Bonnet Cleaning)

This method is similar to dry foam, except that the company sets a large cotton bonnet on your carpet and with a floor polishing buffer machine on top “buffs” the carpet. The rotating motion causes the bonnet to absorb dirt from your carpet. This method is also called bonnet cleaning. Bonnet cleaning is like trying to use a large cotton towel or mop to rub the dirt out of your carpet. It is not very effective

Dry, Absorbent Powder

The dry-compound method spreads a moist, absorbent powder through the carpet. The powder is allowed to dry and then sucked into a vacuum. This method leaves dry sponge particles at the base of the carpet yarn. And because the carpet is not rinsed, this method is not very effective

Hot Water Extraction

This is a fancy way of saying that a hot water cleaning solution under high pressure is forced into your carpet and then sucked out of your carpet.

In a recent Technical Bulletin, Shaw Industries, the world’s largest carpet manufacturer, “recommends the hot water extraction system, which research indicates provides the best capability for cleaning.” You can choose from two different types: Truck-mount extraction, which is done with a large machine mounted in a truck or van. Or Portable extraction, which is done with a small hand-held unit.



According to this bulletin, There is no question: The most effective way to clean carpet is with a hot water unit mounted in a truck. It’s the most powerful cleaning machine on the market and the only machine that cleans the dirt, harmful bacteria, fungus, chemicals, pollen, tobacco residue and dust mites out of your carpet. Some people believe that hot water damages your carpet, but this isn’t true. By washing and then rinsing your carpet with hot water, this would clean your carpet completely, in the same way a person who showers and then rinses off the dirt and the soap will be much cleaner than the person who only takes a sponge bath.

George Washington Slept Here: Historic Home Ownership

By Elaine VonCannon, ABR, SRES, REALTOR



Chances are George Washington did not sleep on your historic home, but in certain parts of Southeastern Virginia, your home could be as old as the dwellings he slept in. To own and restore a historic property, preparation, discernment, and sensitivity are necessary. The rewards of historical home ownership are many.

Financial Advantages of Historic Home Ownership

One of the major benefits of historic home ownership is the stability of resale values. Historic homes generally increase or maintain their worth over time. Historic homes sell faster when on the market because they are rare. They also attract a very particular type of high-end buyer.

Aesthetics of Historic Home Ownership

The proud historic homeowner is also a part of something bigger -- the rich tapestry of American history. Historic homeowners live in or possess property that is completely unique. These homes have an uncommon design, illustrate a high level of craftsmanship, and are made of high quality, often enduring materials that are not generally utilized in contemporary building.

Community Spirit in Historic Neighborhoods

There is a lower turnover in historic districts. Homeowners in historic districts feel they are truly part of a community. In these districts, it is not uncommon for neighbors to work together to preserve their property values and to build the community spirit.

Preserving the American Way of Life

It is always easier to tear down a part of history and rebuild than it is to restore and rehabilitate part of our American heritage. As a historic homeowner you are a part of the preservation of history. Your historic home has a family tree and an ancestry and you and your family become an integral thread in the fabric of time. Sometimes historic homeowners receive recognition by restoring the right home with a sense of integrity. The home tells the tale of a place and time people want to remember. By preserving and restoring the historic property, you have the opportunity to educate people about a period in American history. Often historic homeowners report many different kinds of treasures uncovered in the yard, basement, or attic of their property.

Historical Home Restoration

The work of restoration requires time, skill, and dedication. Many historic homeowners love this challenge, and are willing to give the time and energy it takes to complete a project of this scale. It takes elbow grease, perseverance, patience, sweat, tears and most of all -- money and a budget. Upkeep on historic homes is continual. When repairing damages in historic homes, replace with materials that match originals as closely as possible. Once you become part of the historic preservation community, it pays to investigate and research the resources available. Network with local restoration artists, architects and contractors, especially those familiar with the time period of your area. Visit salvage yards and antique stores to find windows, bathtubs, furniture, or other items for your historical home. Research the time period, history, and architectural style of your home so that as you rehabilitate the property everything originates from or at least replicates the correct period.

Structural Changes in Historic Homes

Exercise caution with design changes, additions or demolition. Always maintain the original scale and proportion of doors and windows to the building. Preserve the number of panes in the windows and the dimensions of columns. Any architectural elements should be replaced with matched materials. For example, wood columns should not be replaced by iron ones. Be prepared to upgrade electrical, plumbing and plaster.

Exterior Changes in Historic Homes

Many historic districts have strict guidelines owners must follow in order to maintain and protect the neighborhood and the historic homes. Learn about acceptable paints or exterior coverings (vinyl siding is not usually a possibility). Know which curtains and shutters are appropriate. Do not alter the original landscaping if possible. Leave the yard a yard instead of converting it into a driveway. Additions must match scale, size and style of the original structure. Do not change the pitch of the roof.

Interior Renovations

Windows and bathtubs might not have to be replaced, see if the originals can be re-glazed. Honor the signature elements that are indicative of your home's particular style. Be gentle when cleaning surfaces. Hire a professional architect and contractor with a background in restoration and rehabilitation. Be sure these professionals are trustworthy and communicate well.

The National Register of Historic Places

This register provides citations that confirm the historical significance of a property. Created in 1966 by the National Preservation Act, this resource has a database with 79,000 districts, sites, buildings and homes listed. Areas with particular scenic, cultural or tourism value usually have design control regulations. Visit <http://www.cr.nps.gov/nr/> to learn about the preservation ordinances in the area where you plan to buy a historic home.

I help buyers in Southeastern Virginia locate historic properties. I encourage homebuyers to reclaim our American heritage to build civic pride, revitalize downtown areas, create economic growth and development, generate tourism, and educate local residents. Use national, state, local and private resources to help preserve your historic property. If you are looking in areas of Virginia such as Williamsburg, Gloucester, Smithfield or surrounding counties, I can be especially helpful. Call me at 757-288-4685 or e-mail vmor1@cox.net to initiate a search for the right historic home for you.

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"Glass, china and reputation are easily cracked, and never well mended."

--Benjamin Franklin

From Elaine's Desk....



Q: Dear Elaine,

We are getting ready to move into a home that has a crawl space after living for 20 years in a house that was built on a slab. My friends have been telling me all these horror stories about moisture under the house. Do you have any advice for us?

-Bruce E. Shea
New Kent, Virginia

A: Dear Bruce,

Start by making sure that the home you are purchasing has a layer of sand under it and a plastic moisture barrier. The plastic should have a few very small holes in it, in order to allow the plastic to breathe. A good termite and moisture company or contractor can do this if you choose not to do it yourself. Another recommendation of mine is to keep bushes, shrubs and other plants trimmed at least 5 inches from the house as well as to have a 6-inch buffer of pea-gravel between the house and any mulch or landscaping areas. This is vital to keep moisture away from the house. Drains and gutters are very important to divert moisture from your home. The black plastic drain extenders that go on the end of the gutter spouts are a great idea.. There is no reason to be nervous. If you have any electric or plumbing work to be done, it is a lot easier to do it in a crawlspace than if the house is on a slab. The base of your home is all about personal preference, there is really no right choice.

Elaine

Each issue (every two months) Elaine will answer your questions on real estate related topics. If Elaine chooses your question to appear in *The Home Edition*, you will receive a \$50 gift certificate to the restaurant of your choice. Please send questions to:

voncannonrealestate@cox.net

From Nana's Kitchen:

INGREDIENTS:

1 pound butter
1 rib celery, finely chopped
2 bunches green onions, finely chopped, about 2 cups
1 bunch parsley, fine chopped
3 tablespoons Worcestershire sauce
1/2 to 1 teaspoon Tabasco sauce
1/2 cup Pernod, Anisette, or Herbsaint
1 1/4 cups seasoned bread crumbs
4 dozen in their shells
rock salt



Oysters Rockefeller

PREPARATION:

Melt the butter in a large skillet and add the celery, scallions and parsley. Sauté for 5 minutes, then add the Worcestershire and Tabasco. Reduce heat to medium and cook for 10 minutes. Add the Herb saint or Pernod and bread crumbs; cook for 5 minutes more. Remove the pan from the heat and transfer the mixture to a bowl. Chill in the refrigerator for 1 hour, until cold but not firmly set. Shuck oysters. Discard the top shells; scrub and dry the bottom shells. Drain the oysters. Arrange several oyster shells in baking pans lined with about 1 inch of rock salt. Arrange several pans in advance, if desired. Place 1 oyster in each shell. Heat oven to 375°. Remove the chilled Rockefeller topping from the refrigerator and beat it with an electric mixer to evenly distribute the butter and infuse air into the mixture; transfer the mixture to a pastry bag fitted with a large plain tip. Pipe a tablespoon of the mixture onto each oyster, then bake in a 375° oven for 5 to 8 minutes. Allow about 6 oysters for each guest. If possible, bake these in batches of 6 in oven-safe pans, so each person can be served a pan of hot Oysters Rockefeller right out of the oven.

Recipe taken from Southern US Cuisine