



Case Study: REIT



A highly successful, privately held Real Estate Investment Trust (REIT) focused on the commercial retail sector.

A mid-sized regional REIT, focused on the retail commercial sector, sought to take advantage of a strong buyer's market to not only raise the profile of its portfolio, but also provide greater returns to its shareholders by driving more top-line revenue. The aggressive “buy low and sell high” growth strategy consisted of selling up to 20 small retail out-parcels (with an average value of \$2.5 million) and using the proceeds to purchase a large retail complex in the Southwest region of the country (with a value of \$100 million). Central to its plan was the utilization of a series of 1031 exchanges, which would help the REIT defer the gain on the sale of its out-parcels and thus increase the amount of cash available to acquire the larger and more profitable retail complex.

Nationwide Exchange Services

The Challenge

While the investment opportunity and plan were fully endorsed by the REIT's management team, the size, scale and complexity of the series of sales in the exchange represented a departure from those they had successfully implemented in the past. In addition, a recent downturn in the commercial real estate sector in that region, combined with other challenging economic conditions, including constricted liquidity in the lending market, produced a climate of uncertainty for large real estate transactions. To ensure the plan's success, as well as address any potential concerns, the REIT's management team identified the need to work with a Qualified Intermediary (QI) that offered state-of-the-art business practices and services, which included:

- A greater expertise in conducting complex, multimillion-dollar real estate exchanges.
- An increased level of funds security, transactional transparency and regulatory compliance.
- A more flexible and streamlined approach to document creation and management.
- A relationship and open communication with the REIT's in-house counsel and tax advisers.
- An ability to work with top-tier banking institutions.

The NES Solution

NES put together an industry-leading Account Team with outstanding 1031 industry expertise and years of REIT industry experience to address the needs of this transaction. After receiving the business brief from the client, the Account Team designed a customized exchange solution that streamlined and safeguarded all of the critically important processes associated with conducting this complex exchange.

- **A Smarter Exchange Agreement.** Working closely with the REIT's in-house counsel and tax advisers, NES drafted a customized Exchange Agreement. This Exchange Agreement contained provisions for the disposition of multiple properties, thus reducing the time required to create separate agreements or amendments for each of the 20 properties to be exchanged. In effect, this allowed the REIT to focus on the deal, rather than time-consuming paperwork.
- **Solid Funds Security.** Knowing that the safety and liquidity of the exchange funds were of paramount importance to the REIT's management team, NES established a Qualified Escrow account, with one of its top-tier custodial banking partners, to hold the proceeds from the sale of each property. Along with the bankruptcy protection afforded by the Qualified Escrow account, the REIT's funds were invested in a secure, liquid money market account. This afforded the REIT an opportunity to work with one of its preferred credit banks.
- **Timely Transactional Transparency.** Keeping track of all of the exchange documentation, as well as the account funds generated from the sale of each of the out-parcels, was also vitally important to the REIT's management team. To provide a greater level of transactional visibility, NES utilized its innovative web-based customer portal. On this fully secure, password-protected website, the REIT's management team was able to view all of its account information and transactions 24/7 – from balances to interest posting, signed exchange agreements to the status of the exchange.
- **Full Compliance. Full Reporting.** Protecting against any form of financial exposure was a key concern of the REIT's management team, especially given the size, scope and complexity of its exchange. NES' SAS 70 Type II certification gave the REIT's management team the assurance that the business processes and controls employed by NES are compliant with all of the IRC Section 1031 regulations, as well as SOX 404. Moreover, NES could provide full audit trail reporting of the transaction.

The Results

The customized exchange solution developed by NES provided the REIT with a cost-effective, streamlined and secure exchange, as well as the value-added support and confidence that the REIT's management team sought in conducting their multi-property and complex disposition plan.

- **Innovative Approach.** Recent IRS private letter rulings on REIT "safe harbor" limitations state that a like-kind exchange does not count as a sale against the historical asset disposition limits. Thus, this REIT was able to dispose of any number of properties representing a sizable percentage of the adjusted cost bases of all its assets.
- **More Buying Power.** By using a Forward Exchange, this REIT was able to bundle the proceeds from a group of relinquished properties, which created additional buying power for the purchase of a more desirable replacement property.
- **Cost-Effective Program.** By using a Forward Exchange, this REIT realized the advantages of a streamlined transaction with lower service fees while earning interest on its exchange funds.

The capital recycling chart below illustrates the additional buying power the REIT realized by implementing a 1031 exchange of this scope and complexity with NES.

REIT Example	Utilizing 1031 Exchange
Sale of Portfolio	
Sales Price of Out Parcel	\$2.5M
Tax Basis	\$500K
Gain on 20 Properties	\$40M
Capital Retained in the REIT (95%) to be used as part of equity in an acquisition	\$38M

Unmatched Expertise – Matched Only By Our Best Practices

Every year, NES conducts thousands of successful 1031 exchanges of varying forms and complexities across a wide spectrum of industries. NES Exchange Specialists are supported by an in-house legal team, unparalleled in the 1031 industry. Our highly experienced attorneys are leaders in their field and include a former IRS National Office official who was instrumental in the development of important IRS 1031 guidance and is a nationally recognized author and speaker on 1031 exchange issues. This marketplace expertise along with our fully compliant business practices and processes have set new standards of excellence in the 1031 industry.

These best practices add immeasurable value to every client’s exchange, addressing the critically important areas of funds security, transactional transparency, and voluntary and regulatory compliance. All of which helps explain why we conduct more types of exchanges for more Fortune 500 companies than any other QI in the 1031 industry.

The NES Difference

- NES offers a comprehensive set of 1031 exchange and LKE Program solutions with the highest level of expertise in the industry.
- NES annually subjects its business practices, financial policies and customer provisions to an independent audit to ensure the highest level of funds security, transactional transparency and compliance.
- NES is the only SOX 404 compliant provider for Section 1031 exchanges.
- NES is the only QI to be awarded SAS 70 Type II certification (the same level of audit and certification required to obtain a federal bank charter).
- NES’ innovative technology platform provides full audit and reporting capabilities while providing 24/7 visibility of all account transactions to each client through a password-protected website.
- NES carries errors and omissions and fidelity bond coverage on every transaction.

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