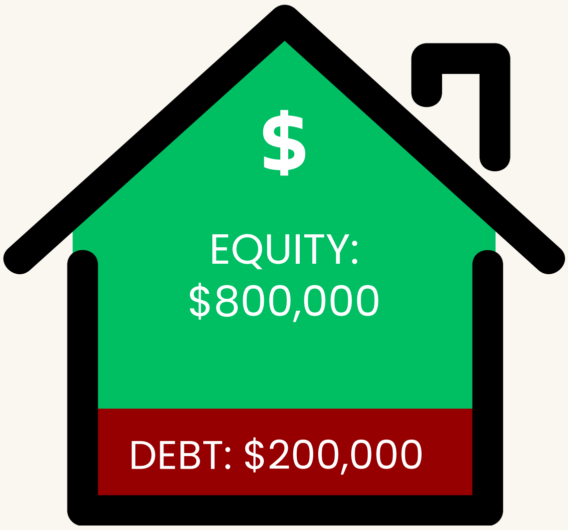
1031 REFI + DST STRATEGY

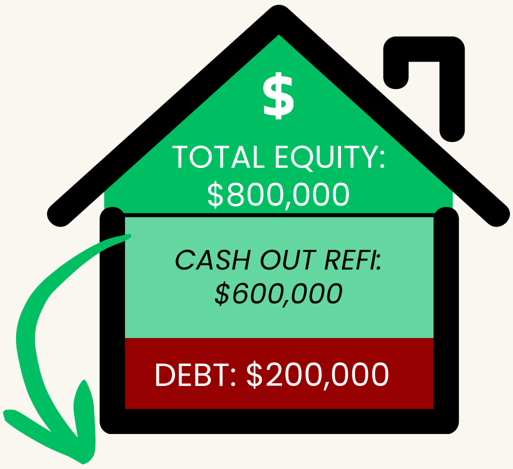
Simplified Step-by-Step

STEP 1: ASSESS VALUE



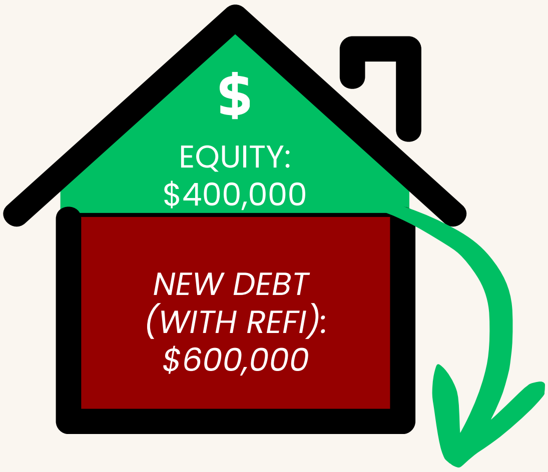
VALUE: $1,000,000

STEP 2: REFINANCE



Cash Out Refi (60%): **$400,000**
($600,000 - $200,000 Debt)

STEP 3: LIST & SELL



Sale Proceeds: $400,000

STEP 4: 1031 INTO DST

SALE PROCEEDS TO INVEST:
$400,000

DELAWARE STATUTORY TRUST (DST)

Maintain 1031 Tax-Deferral Benefits

Shift to Passive Income Model

THE KATALYST TEAM
626-969-2500
TheKatalystTeam.com
TheKatalystTeam@ETHOSLending.com

ETHOS
LENDING

1031 REFI + DST STRATEGY

FAQ Sheet

What is a Delaware Statutory Trust (DST) and why does it qualify for a 1031 exchange?

A DST is a legal entity that allows you to own fractional interests in institutional-grade commercial real estate. The IRS recognizes DST beneficial interests as "real property," making them eligible for 1031 exchange treatment. This allows you to transition from active property management to passive ownership while maintaining your 1031 tax deferral.

Can I refinance my investment property before doing a 1031 exchange into a DST?

Yes. A cash-out refinance prior to a 1031 exchange is permissible as long as it serves a legitimate business or investment purpose - not solely to avoid taxes. The timing between your refinance, use of proceeds, and eventual sale is critical to maintaining IRS compliance.

What qualifies as a legitimate business purpose for the refinance?

Acceptable uses include:

- Purchasing additional investment property
- Diversifying into stocks, bonds, REITs, or private equity
- Funding a business venture
- Making improvements to the property
- Restructuring existing debt
- Covering business or operational expenses

How long should I wait between refinancing and selling my property?

Generally:

- Under 3 months: Highly risky; likely viewed as tax avoidance
- 3-6 months: Somewhat risky; requires strong justification and documentation
- 6-12 months: Stronger position with documented business purpose
- 12+ months: Safest separation, very low IRS challenge risk

THE KATALYST TEAM

626-969-2500

TheKatalystTeam.com

TheKatalystTeam@ETHOSLending.com

ETHOS LENDING

1031 REFI + DST STRATEGY

FAQ Sheet

What happens if I refinance too close to my eventual property sale date?

If the IRS determines your refinance was primarily designed to extract equity immediately before the sale, the cash proceeds may be reclassified as "boot" (taxable cash received), creating a capital gains tax liability even if the 1031 exchange itself remains valid.

Can I take cash out at the time of closing on my sale?

Yes, but any cash taken at closing is taxable and treated as "boot." This won't invalidate your 1031 exchange - the remaining proceeds can still be exchanged tax-deferred - but you'll owe capital gains tax on the cash amount received. This is why the refinance strategy happens before the sale: it allows you to access equity tax-free as loan proceeds rather than taking taxable boot at closing.

What documentation should I maintain to demonstrate compliance?

- Loan documents clearly stating business purpose
- Records showing how refinance proceeds were used
- Timeline showing separation between refinance and sale
- Documentation of business or investment activities funded by proceeds
- Communications with your tax advisor regarding the strategy
- Do not mix refinance proceeds with 1031 exchange funds, and ensure all exchange proceeds remain with your Qualified Intermediary.

Consult with your tax adviser and 1031 company to ensure proper compliance.

THE KATALYST TEAM

626-969-2500

TheKatalystTeam.com

TheKatalystTeam@ETHOSLending.com

ETHOS LENDING

1031 REFI + DST STRATEGY

FAQ Sheet

Is the interest on my refinance loan tax deductible?

Generally yes, if the loan proceeds are used for business or investment purposes. Interest is not deductible if used for personal reasons. Interest deductibility is governed by IRC §163(d). If you don't have sufficient investment income to deduct the interest in the current year, it may be carried forward to future tax years. Consult your tax advisor for your specific situation.

Is the early refinance + DST 1031 a common strategy?

A cash-out refinance before a 1031 exchange into a DST is a legitimate strategy for sophisticated investors when structured properly. However, timing, purpose, and documentation are critical. This strategy requires careful planning and coordination between your mortgage advisor, tax professional, 1031 Qualified Intermediary, and DST sponsor.

What are the main risks or limitations of DST investing?

Illiquidity: You typically cannot sell your interest until the DST sponsor sells the underlying property (usually 5-10 years)
No control: The sponsor makes all management and operational decisions
Distribution risk: Income distributions depend on property performance and are not guaranteed
Fees: DST offerings include sponsor fees and ongoing management costs

This is why DST investing is often most suitable for those seeking simplified, passive income and not needing access to this capital in the short term.

SUMMARY

This strategy allows you to have the best of both worlds - tax-free cash now, and a tax-deferred transition into passive income later.

THE KATALYST TEAM

626-969-2500
TheKatalystTeam.com
TheKatalystTeam@ETHOSLending.com

ETHOS
LENDING