Zero Cash Flow Properties

Hypothetical Example

Inland
Private Capital Corporation

A Potential Solution to Cover 1031 Exchange Debt Requirements

Zero cash flow properties (zeros) are investment structures that help investors meet the 1031 exchange requirements of spending all of the equity (proceeds) from the sale of the relinquished property on a replacement property, and assume a loan on the replacement property that is equal to or greater than the amount of debt on the loan from the relinquished property. Zeros are typically highly leveraged commercial real estate assets with long-term leases backed by investment-grade tenants. These property types have debt service obligations that are paid from the net operating income (NOI) generated by the properties, thus offering no cash flow to the investor. Investors looking to cover 1031 exchange replacement requirements might find a zero an attractive solution.

Hypothetical Example*

An investor is coming out of a moderately leveraged property sale with $400,000 equity left for reinvestment. To fulfill the debt requirement of the 1031 exchange and avoid tax implications, the sum of the cash invested and the debt placed on the replacement property must be equal to or greater than the sum of the cash invested and debt placed on the relinquished property. The investor chooses two replacement property investments, one with an average loan-to-value ratio (LTV), the second is a zero cash flow investment with a high LTV. Here's how a zero would be utilized to meet this investor's needs.

Sale of Relinquished Property	
Total Sales Proceeds	$1,000,000
Mortgage Balance (Debt Remaining)	$600,000
Net Sale Proceeds (Equity Available for Reinvestment)	$400,000
Replacement Property Investments	
Investment A	
LTV	50.92%
Equity Invested	$350,000
Total Investment A Amount (Equity/1-LTV Percent) ($350,000/1-0.5092)	$713,121.43
Debt Assumed on Investment A ($713,121.43 – $350,000)	$363,121.00
Investment B (Zero)	
LTV	83.60%
Equity Invested	$50,000
Total Investment B Amount (Equity/1-LTV Percent) ($50,000/1-0.8360)	$304,878.04
Debt Assumed on Investment B ($304,878.04 – $50,000)	$254,878.04
Total Investment Amount ($713,121.43 + $304,878.04)	$1,017,999.47
Debt Assumed on Total Investment ($363,121.00+ $254,878.04)	$617,999.04
This hypothetical example satisfies 1031 exchange requirements with the total equity invested being equal to or greater than the net sales proceeds from the relinquished property, and the Debt Assumed on the Total Investment being greater than the debt on the relinquished property.	

*Note this is a simplified example intended to solely illustrate the way in which a zero cash flow property investment can satisfy the debt requirements of a 1031 exchange transaction and is not intended to provide a recommendation of investment or to provide tax advice. **Please see reverse side for important disclosures.**

Important Risk Factors

- No public market currently exists, and one may never exist, for the interests of any IPC-sponsored program. The purchase of interests in any IPCC-sponsored program is suitable only for persons who have no need for liquidity in their investment and who can afford to lose their entire investment.
- IPC-sponsored programs offer and sell interests pursuant to exemptions from the registration provisions of federal and state law and, accordingly, those interests are subject to restrictions on transfer.
- There is no guarantee that the investment objectives of any particular IPC-sponsored program will be achieved.
- The actual amount and timing of distributions paid by IPC-sponsored programs is not guaranteed and may vary. There is no guarantee that investors will receive distributions or a return of their capital.
- Investments in real estate are subject to varying degrees of risk, including, among other things, local conditions such as an oversupply of space or reduced demand for properties, an inability to collect rent, vacancies, inflation and other increases in operating costs, adverse changes in laws and regulations applicable to owners of real estate and changing market demographics.
- IPC-sponsored programs depend on tenants for their revenue and may suffer adverse consequences as a result of any financial difficulties, bankruptcy or insolvency of their tenants.
- IPC-sponsored programs may own single-tenant properties, which may be difficult to re-lease upon tenant defaults or early lease terminations.
- The acquisition of interests in an IPC-sponsored program may not qualify under Section 1031 of the Internal Revenue Code of 1986, as amended (the "Code") for tax-deferred exchange treatment.
- Disruptions in the financial markets and challenging economic conditions, including those resulting from the novel coronavirus and resulting pandemic, could adversely affect the operating results of properties owned by IPC-sponsored programs and the ability of such programs to service the indebtedness on their properties.

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