

Opportunities Beyond Traditional 1031 Exchanges



What is a 1031 Exchange?

Named after section 1031 of the U.S. Internal revenue code, a 1031 exchange is a procedure that allows an owner of appreciated real estate to exchange that property for an alternative “like-kind” property while deferring capital gains.

CAPITAL-GAINS TAX DEFERRAL AND OTHER BENEFITS

When a real estate investor wants to sell one property and buy another, the primary benefit of doing so through a 1031 exchange is the ability to **defer capital gains taxes**. Thus, the higher the capital gains bill that an investor faces, the more they would potentially gain.

While real estate investing offers many benefits, appreciated commercial property can also present investors with difficult choices when selling implies a large capital-gains tax bill. Knowing how to invest in a tax-efficient manner can have a significant impact on the value of those benefits, and 1031 exchanges are one of the most tax-efficient investment vehicles available to real estate investors.

A 1031 EXCHANGE MAY ENABLE INVESTORS TO:

 Increase purchasing power in the replacement property by freeing up capital

 Diversify assets

 Consolidate several properties into one, or divide one into several

 Gain the flexibility of owning shares in a portfolio of real estate in place of direct property ownership

 Sell a real estate investment with a low cost basis

 Bequeath their assets and take advantage of the step-up in tax basis

 Move to a passive role, reduce ongoing property management burdens or switch to a managed property

 Seek a property with better return prospects

 Capitalize on the value of appreciated assets

 Reset the depreciation clock

 Maximize the amount of wealth working for them

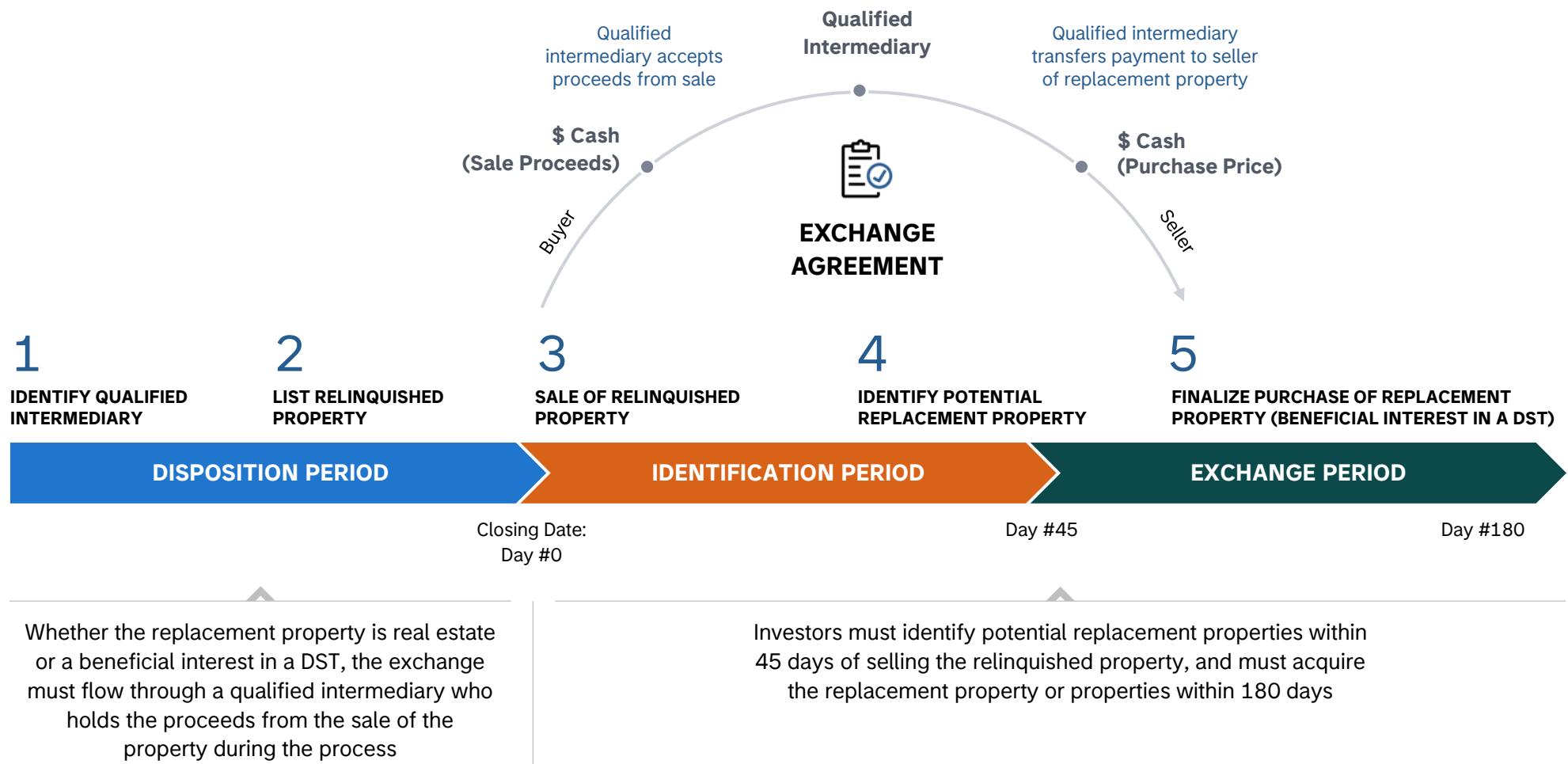
A 1031 EXCHANGE MAY HAVE:

- A high minimum investment
- Low liquidity for at least three years (potentially longer)
- Require the help of tax, real estate and potentially estate planning professionals
- Single property risk
- Nonpermanent solution
- Difficulty around estate planning (divisibility among heirs)

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The 1031 Exchange Cycle



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Exchanging Into a Delaware Statutory Trust

Section 1031 Allows Not Only Direct Property Exchanges, But Also Exchanges From a Single Property Into a Delaware Statutory Trust (DST).



WHAT IS A DST?

BENEFICIAL OWNERSHIP INTEREST IN INSTITUTIONAL-QUALITY REPLACEMENT PROPERTY

A DST is a trust that owns large, institutional-quality property

The IRS has ruled that beneficial interests in a DST may be treated as direct interests in replacement property for purposes of IRC Section 1031

Investors receive a stated income stream backed by a guaranteed fixed master lease

WHO IS A DST POTENTIALLY APPROPRIATE FOR?

A DST MAY BE PARTICULARLY APPROPRIATE FOR INVESTORS WHO ...

Are unsure they can find and acquire replacement property within the stringent time requirements of 1031 exchanges

Have grown tired of actively managing their own investment property and would prefer to switch to a more passive role

Seek access to institutional-quality real estate that they may not be able to acquire directly

BENEFITS OF EXCHANGING INTO A DST

BY EXCHANGING INTO A DELAWARE STATUTORY TRUST, INVESTORS GAIN ...

Access to institutional-quality real estate

Deferral of capital gains taxes

Professional property management

Potential passive rental income

Pre-arranged financing (if applicable)

Potential for appreciation

Ease in complying with IRC Section 1031 requirements

Tax benefits of traditional investment in real estate

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The UPREIT Process

The UPREIT process uses two distinct steps—the 1031 exchange and the 721 exchange. Taken together, this allows investors the ability to convert their investment property ultimately into operating partnership units of a nationally syndicated REIT portfolio.



A TWO-STEP PROCESS

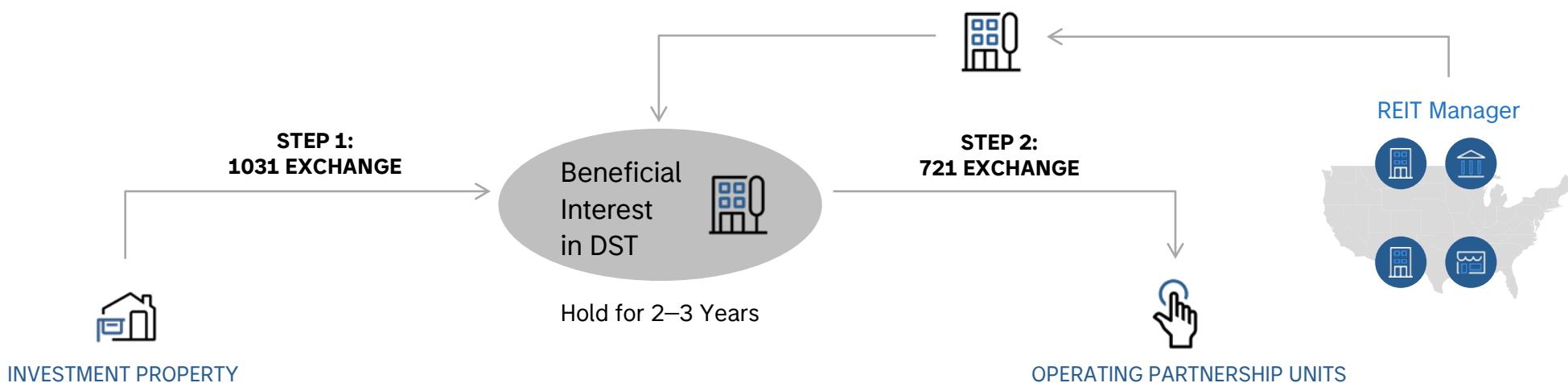
Investors without institutional-quality real estate can combine 1031 and 721 exchanges. Neither step triggers capital gains taxes.

1

1031 exchange: An investor swaps their original, nonqualifying property for shares in a Delaware statutory trust (DST)

2

721 exchange: The REIT can exercise an option to purchase one or more properties held in the DST at fair market value, for which the investor receives OP units in the REIT. The REIT typically owns a diversified portfolio of properties across asset types and geographic locations

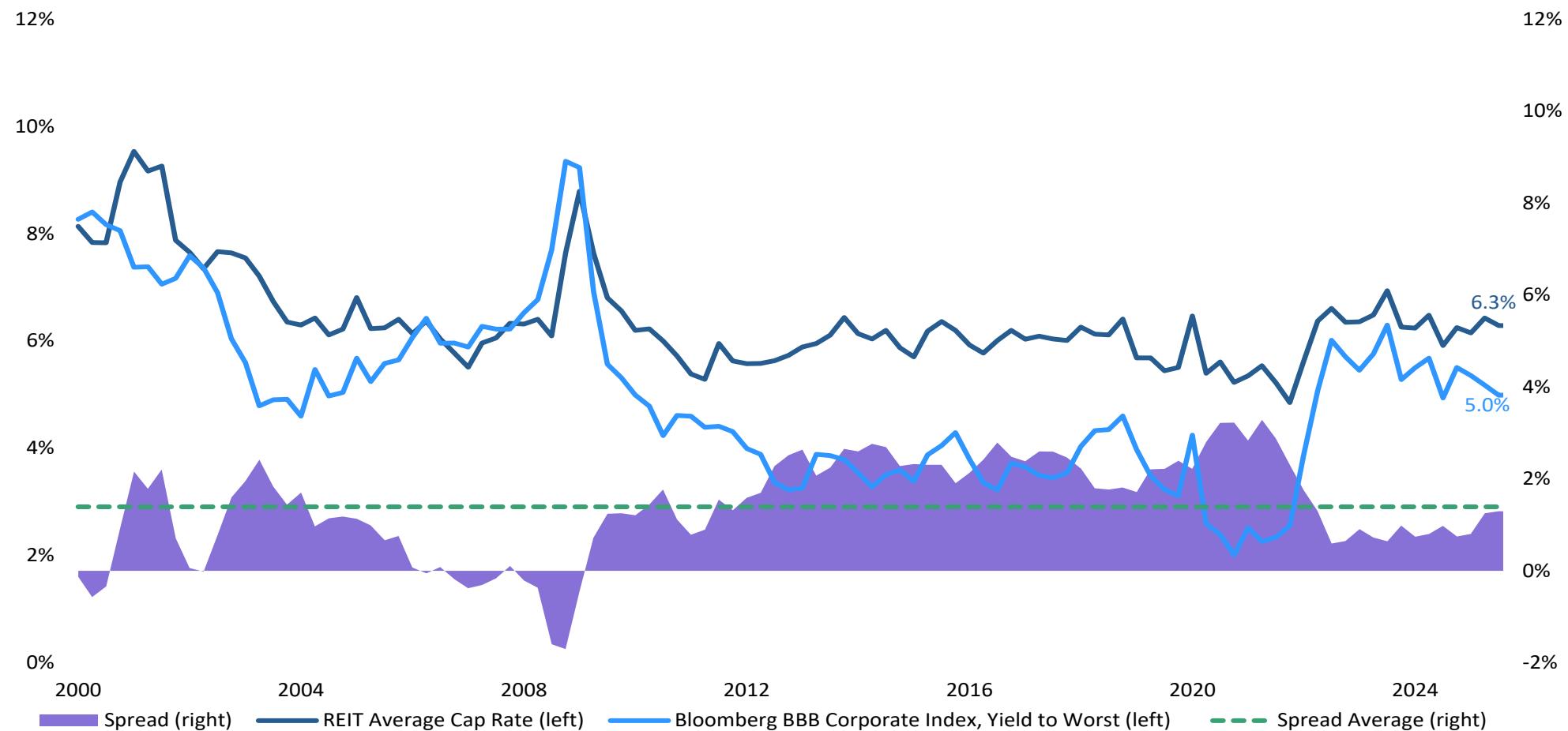


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REIT Performance

AS OF DECEMBER 31, 2025



Source: Morgan Stanley Wealth Management GIO, Bloomberg.

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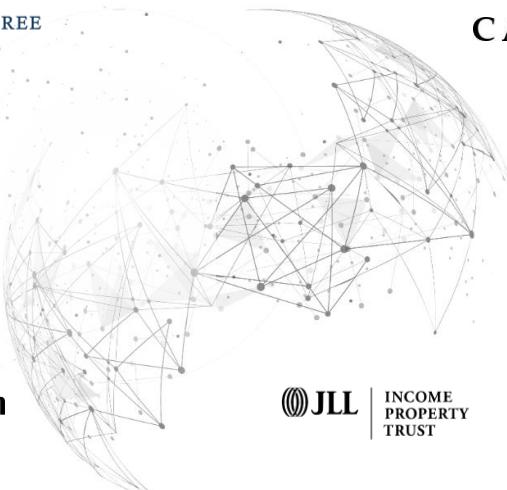
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Investing in **Commodities:** Commodity prices may be affected by factors such as supply and demand, government policies, domestic or international political and economic events (including war or terrorism), changes in interest and exchange rates, trading activity in commodities and related contracts, pestilence, technological developments, weather, price volatility, and liquidity constraints. Physical precious metals are speculative, non-regulated products that may experience short- and long-term price volatility. Precious metals do not make interest or dividend payments and therefore may not be appropriate for investors who require current income. Precious metals must be stored, which may impose additional costs on investors.

Master Limited Partnerships (MLPs): Investments in MLPs are subject to the risks generally applicable to companies in the energy and natural resources sectors, including commodity price fluctuations, supply

and demand imbalances, resource depletion and exploration risk. MLPs also carry interest rate risk and may underperform in rising interest rate environments. In addition, MLP funds accrue deferred income taxes on net operating gains and capital appreciation; as a result their after-tax performance could differ significantly from that of its underlying assets.

Exchange Funds are private placement vehicles that enable holders of concentrated single-stock positions to exchange those stocks for a diversified portfolio. Investors may benefit from greater diversification.

Alternative investments are often speculative and include a high degree of risk. Investors can lose all or a substantial amount of their investment. They are appropriate only for eligible, long-term investors willing to forgo liquidity and put capital at risk for an indefinite period. They are often illiquid, may employ leverage, short-selling, or other speculative practices that increase volatility and risk of loss, and may require large minimum investments and initial lock-ups. Alternative investments may also involve complex tax structures, tax-inefficient investing, and delays in distributing important tax documents. Clients should consult their own tax and legal advisors, as Morgan Stanley Wealth Management does not provide tax or legal advice. They also typically carry higher fees and expenses than traditional investments, which can reduce overall returns.

Sector investments, due to their narrow focus, tend to be more volatile than broadly diversified investments. **Non-diversified portfolios:** Portfolios that hold a concentrated number of securities may experience greater overall declines when those securities lose value compared with more diversified portfolios. Portfolios that invest heavily in one or a few industry sectors are more vulnerable to price fluctuations than those diversified across a wider range of sectors.

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