

Like-Kind Exchanges (Form 8824)

IRC §1031 and IRS Publications 544 and 550

No gain or loss is recognized if property held for productive use in trade or business or for investment is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment.

Definition. Like-kind property means property of the same nature or character, not necessarily of the same grade or quality. For example, improved real estate can be exchanged for unimproved real estate.

Exchanges can include business for business, business for investment, investment for business or investment for investment property. Property held for personal use, inventory and securities do not qualify under the like-kind exchange provisions.

Requirements. Nonrecognition treatment for like-kind exchanges is mandatory rather than elective. A taxpayer who wants to recognize a realized gain or loss must structure the transaction around the statutory requirements for a like-kind exchange.

To qualify as a tax-deferred, like-kind exchange, all six of the following conditions must be met:

- 1) Both the property traded and the property received must be held by the taxpayer for business or investment purposes.
- 2) The property must not be held for sale to customers, such as inventory or merchandise.
- 3) There must be an exchange of like property. In general, any kind of real estate is treated as of like kind with other real estate. By contrast, different kinds of personal property (for example, equipment and vehicles) are not treated as like kind. Tangible and depreciable personal property may be either "like kind" (based on individual facts and circumstances) or "like class" (an objective test).
- 4) Exchanges of intangible personal property depend on the nature or character of the rights involved. Stocks, bonds, notes and other securities do not qualify for a like-kind exchange. The goodwill of any business will not qualify in a like-kind exchange.
- 5) The property to be received in an exchange must be identified in a written agreement within 45 days after the transferred property is surrendered.
- 6) The property in the exchange must be received on or before the earlier of:
 - 180 days after the transfer of the property given up, or
 - The due date (including extensions) for the tax return year in which the transfer of the property given up occurs.

Like-kind exchanges using qualified intermediary. If property is transferred through a qualified intermediary, the transfer of the property given up and receipt of like-kind property is treated as an exchange. This rule applies even if the taxpayer receives money or other property directly from a party to the transaction other than the qualified intermediary.

Liabilities

All liabilities transferred to the other party in an exchange are netted against all liabilities transferred to the taxpayer. The taxpayer is treated as receiving "boot" only if relieved of greater liabilities than those assumed.

Boot

Property that is not like-kind property (including cash) is known as "boot." If the transferee either assumes a liability or takes property subject to a liability, the amount of the liability is treated as boot received by the transferor.

The receipt of boot will cause a realized gain on an exchange to be recognized. Gain is realized if the FMV of the property received exceeds the tax basis of the property given. The amount of gain to recognize is the lesser of the boot received or the realized gain. The realized gain is the maximum gain that can be recognized in an exchange.