Exchanges -
Concepts and Tax Implications

Course Description

While tax reform visions have changed the tax on profits realized from the disposition of real estate, investors still seek escape hatches from the capital gain tax. Tax-deferred exchanges permit the disposition of property often with the taxpayer receiving significant cash but without the payment of any tax. Functionally, an exchange is a bridge over the normally taxable event of moving from one property to another. This course alerts the practitioner to the different planning opportunities that surround exchanging. Participants will be able to identify, analyze, and handle effectively the complex tax problems that arise under 1031. This understanding will be directly applied to the structuring and audit survival of multi-party and delayed exchanges.

Completion Deadline & Exam: This course, including the examination, must be completed within one year of the date of purchase. In addition, unless otherwise indicated, no correct or incorrect feedback for any exam question will be provided.

Course Level: Overview. This program is appropriate for professionals at all organizational levels.
CPE Credits: 13 (CPA, EA)
Field of Study: Taxes
Prerequisite: General understanding of federal income taxation.
Advanced Preparation: None

Course Learning Objectives

Chapter 1: Introduction - Section 1031

1. Identify factors that determine the popularity of exchanging, specify tax law changes influencing exchange popularity and the impact of current capital gains rates, recognize the capital gain rate "baskets" and determine the tax treatment of assets in each category.
2. Recognize the differences between exchanges and installment sales and the cost benefits of each, identify several advantages given to exchanging by recent legislation and specify continuing problems that can arise with an installment sale that can act as an impetus for using an exchange.
3. Specify multiple tax benefits of exchanges and the advantages they create over installment sales and determine issues that can be re-solved or facilitated by using a like-kind exchange.

Chapter 2: Section 1031 & Its Function

1. Determine the conceptual changes made to §1031 by the TRA ’84, TRA ’86, the Revenue Act of 1987, and the RRA ’90 and specify the current provisions of §1031 by:
   a. Identifying the differences in §1031 from the general rule of taxation under §1001;
   b. Recalling its legislative evolution; and
   c. Recognizing the original Congressional rationale of §1031 contained in the concepts of continuity of investment and administrative convenience.
2. Specify instances where the IRS may assert an unintended mandatory application of §1031.

Chapter 3: Statutory Requirements & Definitions

1. Specify the elements §1031 and how these elements conceptually differentiate a like-kind exchange from a sale.
2. Identify excluded property types from qualified property types by determining the meaning of the phrases “held for productive use in a trade or business,” “productive use,” and “investment purpose” specifying the impact of time and taxpayer intent.
3. Recognize the state of mind issues in the concept “held for productive use in trade or business or for investment” and how qualifying use can ease qualification, determine the differences between §1031 and old §1034, and cite the same taxpayer requirement and its the unsettled caselaw.
4. Specify the former statutory exclusions from §1031 and the types of property that were specifically excepted.
5. Identify the like-kind requirement as it impacts real estate and personal property, and recognize the former classification systems that permitted clients to exchange like-kind or like-class personal property.

Chapter 4: The Concept of “Boot”

1. Identify “boot” and like-kind property specifying boot's potential impact on nonrecognition and list several examples of boot.
2. Determine taxable "boot," specify the differences between realized gain and recognized gain recalling the limitation on recognition of gain under §1031 that prevents a taxpayer from being taxed greater than if he had sold the property, and recognize taxable “boot’s” net effect.

Chapter 5: The Rules of “Boot”

1. Determine mortgage boot and property boot identifying whether a taxpayer has given or received boot in an exchange and the related tax consequences.

2. Identify the popular and alternate offset rules used to determine net boot, specify techniques to limit net taxable boot such as adjusting mortgages before an exchange and treating closing costs according to R.R. 72-456, and recognize the taxability of gain rule to reflect netting.

Chapter 6: Losses

1. Identify the categories of property received in an exchange and which category is permitted to recognize loss, recognize how avoiding §1031 can allow clients to potentially increase recognizable losses, and determine the tax treatment of non-recognized losses under §1031.

Chapter 7: Basis on Tax-Deferred Exchange

1. Identify the general carryover basis rule to calculate a taxpayer's basis in acquired property by determining its application and specifying the related allocation of basis to multiple properties and boot in an exchange.

Chapter 8: Depreciation, Cost Recovery, MACRS & Recapture

1. Identify property depreciation under §167 particularly as it applies to property used in a taxpayer's trade or business or held for the production of income and the impact of ERTA, TRA '86 OBRA '93, and TCJA determine the changes made by Notice 2000-4, and cite the depreciation requirements of later regulations affecting recovery periods and depreciation methods.
2. Recognize the distinction between land and depreciable improvements, identify the recapture provisions and their impact on the rate to be applied to all or a portion of the gain that would otherwise be recognized.

Chapter 9: Miscellaneous Aspects

1. Specify the holding period of acquired property, identify the character of gain or loss recognized in an exchange, recall the evolution of the installment sale method and the current rules related to exchanges and determine the formula for gain recognized using gross profit, selling price and total contract price under §453.
2. Recognize the danger of exchanges between related parties by:
   a. Specifying the two-year limitation on such exchanges by;
      i. Determining related parties;
      ii. Identifying the special holding period rule;
      iii. Selecting at least three types of dispositions that will not invalidate the nonrecognition treatment on an original exchange; and
      iv. Citing the avoidance exception to §1031; and
   b. Identifying how §§267, 707, 453 and 1239 work together with §1031.

3. Recognize how leveraging can be useful in a §1031 exchange, specify ways to cash out one or more partners out as part of an exchange by a partnership, and choose the proper tax forms to report an exchange.

Chapter 10: Mechanics

1. Recognize a simple test that permits clients and their advisors to determine if an exchange is completely tax-deferred and the components of this test, identify the basic computation figures necessary to economically balance an exchange, and specify methods of evening out to ensure that all parties get the same value as they give.
2. Determine how to balance multiple party exchanges using the in and out test determining net boot, select optimal exchange property to minimize taxable gain, and identify how to use refinancing, the "Coleman" solution, a wrap-around mortgage or a tax-free "cash out" to balance out an exchange.

Chapter 11: Types of Exchanges

1. Identify the mechanics of a two-party and three-party exchange including related variations involving the cash out of a party.
2. Determine the transactional flow of a traditional three-party "Alderson" exchange including variations to the format, recognize the respective parties' tax consequences and recall procedural guidelines to ensure mechanics comply with §1031 provisions.
3. Determine the elements of a three-party "Baird Publishing" exchange and an "Alderson" exchange, specify variations of the "Baird Publishing" exchange and situations when each is the preferred format to use, identify categories of four-party exchanges, and specify when conditions favor the use of a four-party "Coupe" exchange or a four-party "Mercantile Trust" exchange.

Chapter 12: Delayed Exchanges

1. Identify the distinctions between delayed exchanges and delayed closes particularly as to simultaneity, recall the evolution of delayed exchange requirements from the Starker case through the restrictive TRA '84 time limits to the present and the popularity of delayed exchanges and specify unresolved issues for delayed exchanges.
2. Recognize the requirements of the final regulations for delayed exchanges by:
    a. Identifying the effective date for the regulations;
    b. Specify the differences between delayed exchanges and "reverse-starker" transactions;
    c. Determining the delayed exchange identification requirements by:
        i. Specifying the identification and exchange periods;
        ii. Identifying replacement property;
        iii. Specifying requirements to revoke the identification of property;

iv. Recognizing the substantial receipt requirement; and

v. Selecting multiple replacement properties according to the requirements of Reg. §1.1031(a)-1(c)(4)(i)(A); and

d. Identifying whether a taxpayer is in actual or constructive receipt of money by recalling the safe harbors that can be used without risk of actual and constructive receipt.

Chapter 13: Warehousing & Pot Method

1. Identify the purpose of a longtime exchange technique called “warehousing,” specify the procedural aspects of reverse exchanges under R.P. 2000-37 and variables impacting its application, recognize the “pot” method recalling the procedural role of “strawmen,” and determine the role of exchange escrows.

Chapter 14: Accommodators & Intermediaries

1. Identify the differences between an accommodator and an intermediary, determine how using such parties can facilitate exchanging by avoiding certain holding problems, multiple parties and properties, and transfer difficulties, and recognize a sale and lease-back transaction and associated exchange complications.