IRB 2017–33
August 14, 2017

ACTION ON DECISION

Subject: Estate of George H. Bartell, Jr. v. Commissioner, 147 T.C 140 (2016)

Issue: Whether Taxpayer's sale and acquisition of business property qualifies as a like-kind exchange under I.R.C. § 1031 even though 17 months before Taxpayer engaged in the purported exchange, an accommodating party facilitating the transaction acquired title to the replacement property and Taxpayer acquired the benefits and burdens of ownership of the property.

Discussion: Taxpayer, intending to engage in a like-kind exchange, entered into an agreement with Exchange Facilitator (EF) to purchase Replacement Property (RP) from Seller. EF acquired title to RP on August 1, 2000, after which Taxpayer constructed a drug store on RP and, in June of 2001, began leasing RP from EF. In December of 2001, Qualified Intermediary (QI) acquired Taxpayer's business property (RQ), sold RQ to Buyer, and used the sale proceeds to acquire RP from EF and transfer it to Taxpayer. EF held title to RP for 17 months before transferring it to QI and then to Taxpayer.

The Service asserted that Taxpayer acquired RP in August of 2000, not December of 2001, arguing that Taxpayer, not EF, acquired the benefits and burdens of ownership of RP from Seller. *See Grodt & McKay Realty, Inc. v. Commissioner*, 77 T.C. 1221 (1981) (providing principles for a benefits and burdens analysis). Thus, the transaction was not a like-kind exchange; instead, Taxpayer sold RQ in a taxable sale in 2001.

The focus of the Tax Court's opinion was on case law decided before the issuance of Treas. Reg. § 1.1031(k)-1 (the deferred exchange regulations) and, in particular, on the cases that address a taxpayer's use of an accommodating party to facilitate an intended like-kind exchange. The court concluded that *Alderson v. Commissioner*, 317 F.2d 790 (9th Cir. 1963), and *Biggs v. Commissioner*, 69 T.C. 905 (1978), *aff'd* 632 F.2d 1171 (5th Cir. 1980), establish the principle that a third-party exchange facilitator "need not assume the benefits and burdens of ownership of the replacement property in order to be treated as its owner for section 1031 purposes before the exchange." *Bartell*, 147 T.C. at 64. Consequently, the court held that the transaction was a like-kind exchange even though EF did not have the benefits and burdens of ownership of RP and held title to RP for 17 months while Taxpayer oversaw construction on RP.

Section 1031 provides that no gain or loss is recognized on an exchange of certain like-kind business or investment property. Section 1031(a)(3) allows deferred like-kind exchanges, which are exchanges in which replacement property is acquired after, but within 180 days of, the taxpayer's transfer of the relinquished property. Section 1.1031(k)-1 allows taxpayers to use qualified intermediaries and other arrangements to facilitate their deferred like-kind exchanges. Neither § 1031 nor the regulations address exchanges of the type engaged in by the taxpayers in *Bartell*, in which the replacement

property is acquired and "parked" with an accommodating party before the taxpayer's transfer of the relinquished property (a reverse exchange).

Rev. Proc. 2000-37, 2000-2 C.B. 308, *modified by* Rev. Proc. 2004-51, 2004-2 C.B. 294, provides a safe harbor for taxpayers seeking to park relinquished property or replacement property with an exchange accommodation titleholder (EAT) in anticipation of a like-kind exchange. If the safe harbor requirements are met, including that the EAT cannot hold the parked property for more than 180 days, the EAT (and not the exchanging taxpayer) is considered the owner of the property held by the EAT, regardless of who has the benefits and burdens of ownership under a *Grodt & McKay* analysis. Section 3.04 of Rev. Proc. 2000-37 provides that, in transactions in which the requirements of the revenue procedure are not satisfied, "the determination of whether the taxpayer or the exchange accommodation titleholder is the owner of the property…, and the proper treatment of any transactions entered into by or between the parties, will be made without regard to the provisions of this revenue procedure."

A taxpayer meets the requirements of § 1031 only if the taxpayer engages in an exchange of property. Thus, unless the requirements of Rev. Proc. 2000-37 are met, a taxpayer who acquires the benefits and burdens of ownership of Property 1 on Date 1 and sells Property 2 on Date 2 has not engaged in an exchange as required by § 1031. See *DeCleene v. Commissioner*, 115 T.C. 457 (2000).

The case law cited in *Bartell* involves transactions that were consummated prior to the issuance of the deferred exchange regulations and Rev. Proc. 2000-37. For transactions outside the scope of the deferred exchange regulations, the Service does not follow the court opinions that take the view that for § 1031 purposes an exchange facilitator may be treated as the owner of replacement property regardless of whether it has the benefits and burdens of ownership. Similarly, in determining whether a reverse exchange outside the scope of Rev. Proc. 2000-37 meets the requirements of § 1031, the Service will not follow the principle in the court opinions that an exchange facilitator may be treated as the owner of property regardless of whether it possesses the benefits and burdens of ownership. Under Rev. Proc. 2000-37, taxpayers are permitted to use an exchange facilitator (called an accommodating party) and meet the exchange requirements of § 1031 even though, using the principles set out in *Grodt & McKay Realty, Inc.*, the taxpayer acquires the benefits and burdens of ownership of the replacement property up to 180 days before the exchange intended to qualify as a tax-deferred like-kind exchange. Taxpayers that use accommodating parties outside the scope of Rev. Proc. 2000-37 have not engaged in an exchange if the taxpayer, rather than the accommodating party, acquires the benefits and burdens of ownership of the replacement property before the taxpayer transfers the relinquished property. The Service will not follow the Tax Court's opinion in *Bartell* to the extent the opinion provides otherwise.

Recommendation: Nonacquiescence.

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