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**Department of the Treasury**

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Taxpayer =  
State W =  
State X =  
State Y =  
State Z =  
State Y RP =  
State Z RP =  
Year 1 =  
Year 2 =  
x =  
a, b, and c =

y =  
z =  
Date 1 =  
Date 2 =  
Date 3 =  
Date 4 =  
Date 5 =  
\$A =

Dear

This responds to Taxpayer's letter, dated December 11, 2000, requesting a private letter ruling as to the application of § 1031 of the Internal Revenue Code ("Code") to the proposed transaction. Specifically, Taxpayer requests rulings that the transfer of replacement property received in a like-kind exchange to a single-member

limited liability company (LLC) will not violate the requirement under § 1031(a)(1) of the

Code that Taxpayer's replacement property must be held for productive use in a trade or business or for investment after the exchange. These are the applicable facts:

Taxpayer, a State W corporation which has elected to be taxed under subchapter S of the Code, uses the cash method of accounting for maintaining its books and preparing its federal income tax returns. With the consent of the Service, Taxpayer uses an accounting period ending on the thirtieth day of April.

Taxpayer was first organized in Year 1 as a cattle operation. Initially, its assets included x acres of pasture and agricultural land in State W. However, to remain economically viable it has gradually diversified its activities, spreading out the inherent risks of weather, crop variation and commodity pricing. Thus, over the past several years it has engaged in the businesses of a, b, and c. In addition to these various enterprises, Taxpayer purchased a y acre steer-grazing ranch in State X in Year 2.

On Date 1, Taxpayer entered into contract to sell certain unencumbered real property consisting of z acres of land located in State W (the relinquished property or RQ) for \$A. Taxpayer entered into this contract intending to exchange the relinquished property for like-kind replacement property in a transaction that would qualify as a deferred like-kind exchange under § 1031(a)(3) of the Code. On Date 2, Taxpayer executed exchange and escrow agreements with a "qualified intermediary," as that term is defined in § 1.1031(k)-1(g)(4)(iii) of the Income Tax Regulations (hereinafter, "QI"). These agreements prohibited Taxpayer from actually or constructively receiving money or property arising from the transfer of RQ, other than properly identified, like-kind property, prior to the occurrence of the events specified in § 1.1031(k)-1(f) and (g). The escrow and exchange agreements were drafted to meet the requirements set forth in § 1.1031(k)-1.

On Date 3, Taxpayer assigned its rights in the contract of sale of RQ (as amended) to QI and gave written notice of this assignment to the purchaser. At the closing, RQ was deeded directly to the purchaser and all sales proceeds were paid to QI, who deposited the proceeds into a "qualified escrow account" within the meaning of § 1.1031(k)-1(g)(3)(ii). The transfer of RQ was effectuated in a manner that met all the requirements of §§ 1.1031(k)-1(g)(4)(iv)(B) and 1.1031(k)-1(g)(8) Example 4.

Within 45 days after the date on which Taxpayer transferred RQ, Taxpayer identified four replacement properties the aggregate fair market value of which as of the end of the identification period did not exceed 200 percent of the aggregate fair market value of RQ as of the date RQ was transferred by Taxpayer. The identification was in writing, was sent to QI, and unambiguously described the possible replacement properties. Taxpayer met all of the requirements for the identification of replacement property set forth in § 1.1031(k)-1(c).

On Date 4, Taxpayer assigned its rights under a certain agreement to acquire a hotel property located at State Y (one of the properly identified replacement properties and hereinafter referred to as "State Y RP") to QI. Prior to the assignment, Taxpayer gave written notice to the seller of the State Y RP that it was assigning its rights under the agreement of purchase and sale to QI. Before 180 days after the date on which Taxpayer transferred RQ (and before the due date of Taxpayer's federal income tax return for the year in which the transfer of RQ occurred) QI transferred funds from the qualified escrow account to the seller of the State Y RP. The State Y RP was deeded directly to Taxpayer. The assignment, notice, transfer of funds from escrow, and direct deeding with respect to the State Y RP were all completed in a manner that strictly complied with the requirements of §§ 1.1031(k)-1(g)(4)(iv)(C) and 1.1031(k)-1(g)(8) Example 4.

On Date 5, Taxpayer assigned its rights under a certain agreement to acquire a hotel property located at State Z (one of the properly identified replacement properties and hereinafter referred to as State Z RP) to QI. Prior to the assignment, Taxpayer gave written notice to the seller of the State Z RP that it was assigning its rights under the agreement of purchase and sale to QI. Before 180 days after the date on which Taxpayer transferred RQ (and before the due date of Taxpayer's federal income tax return for the year in which the transfer of RQ took place) the QI transferred funds from the qualified escrow account to the seller of the State Z RP. The State Z RP was deeded directly to Taxpayer. The assignment, notice, transfer of funds from escrow, and direct deeding with respect to the State Z RP were all completed in a manner that strictly complied with the requirements of §§ 1.1031(k)-1(g)(4)(iv)(C) and 1.1031(k)-1(g)(8) Example 4.

All proceeds from RQ were reinvested in the State Y RP and State Z RP. Taxpayer holds State Y RP and State Z RP for use in its trade or business or for investment.

The hotel businesses operated on these replacement properties are subject to significant and unique liability risks that can best be managed by holding the properties on which they operate in separate single-asset entities. In addition, to satisfy the post-exchange business requirements of the replacement properties, and certain other businesses of Taxpayer, Taxpayer will borrow money using the replacement properties as collateral. The prospective lenders will require each of the replacement properties be held in single-asset entities as a condition to making the necessary loans. To protect its other assets from the risks associated with owning State Y RP and State Z RP and to meet the prospective lenders' requirement that each replacement property be held in a single-asset entity, Taxpayer desires to transfer each replacement property to a separate, wholly-owned State Y limited liability company (State Y LLC). Both State Y LLCs will either elect to be disregarded as entities separate from their owner or will

rely on the default classification rule for single-owner entities under § 301.7701-3(b)(1)(ii). The borrowing will occur in a taxable year subsequent to the taxable year of the exchange. Proceeds from the loan(s) will be used exclusively to advance Taxpayer's business objectives.

Section 1031(a)(1) of the Code provides that no gain or loss will be recognized on the exchange of property held for productive use in a trade or business or for investment if the property is exchanged solely for property of a like kind which is to be held either for productive use in a trade or business or for investment. Under section 1.1031(a)-1(b) of the regulations relating to the meaning of the term "like kind," real property is generally considered to be of like kind to all other real property, whether or not any of the real property involved is improved.

In Rev. Rul. 75-292, 1975-2 C.B. 333, a like-kind exchange of real estate between a taxpayer and an unrelated party was followed by the immediate transfer of the replacement property by the taxpayer to a corporation. This corporation was formed by the taxpayer. The taxpayer exchanged the newly acquired replacement property for the stock of the same corporation in a transaction that qualified for nonrecognition of gain under § 351 of the Code. In the revenue ruling, the Service concluded that the taxpayer did not exchange the real estate for other real estate to be held either for productive use in a trade or business or for investment. Instead, the Service concluded that the replacement property was acquired for the purpose of transferring it to the new corporation, and was not to be held by the taxpayer. As a result, the Service decided, as to that taxpayer, the exchange did not qualify for nonrecognition under § 1031 of the code. See also Rev. Rul. 77-297, 1977-2 C.B. 304; and Rev. Rul. 77-337, 1977-2 C.B. 305.

Under § 301.7701-3(b)(1)(ii), a domestic eligible entity is generally (with exceptions noted) disregarded as an entity separate from its owner if it has a single owner.

Section 301.7701-2(c)(2) provides that, in general, a business entity that has a single owner and is not a corporation (as defined in § 301.7701-2(b)) is disregarded as an entity separate from its owner for federal tax purposes.

In its original submission, Taxpayer expressed concern that the transfer of the each replacement property to a separate wholly-owned State Y limited liability company would violate the holding requirement as applied in Rev. Rul. 75-292. In the present case, however, the transfer by Taxpayer of replacement property to its wholly-owned, single-member LLC will be disregarded and Taxpayer will still be considered the direct owner of such property for federal income tax purposes.

Therefore, based on the facts presented above, we rule as follows:

1. The anticipated transfer by Taxpayer of the of the State Y RP to a single-member, State Y limited liability company, the sole member of which will be Taxpayer, and which will either elect to be disregarded as an entity or will rely upon the default classification rule for single-owner entities under § 301.7701-3(b)(1)(ii), will not violate the requirement under § 1031(a)(1) of the Code that Taxpayer's replacement property be held for productive use in a trade or business or for investment.
2. The anticipated transfer by Taxpayer of the of the State Z RP to a single-member, State Y limited liability company, the sole member of which will be Taxpayer, and which will either elect to be disregarded as an entity or will rely upon the default classification rule for single-owner entities under § 301.7701-3(b)(1)(ii), will not violate the requirement under § 1031(a)(1) of the Code that Taxpayer's replacement property be held for productive use in a trade or business or for investment.

No determination is made by this letter whether the described transaction otherwise qualifies for deferral of gain realized under § 1031. We express no opinion, except as specifically ruled above, as to the federal tax treatment of the transaction under any other provisions of the Code and regulations that may be applicable or under any other general principles of federal income taxation. Neither is any opinion expressed as to the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction(s) that are not specifically covered by the above ruling.

This ruling is directed only to the taxpayer(s) who requested it. Section 6110(k)(3) of the Code provides that it may not be cited as precedent.

Sincerely yours,  
Associate Chief Counsel  
(Income Tax & Accounting)

By: Robert M. Casey  
Senior Technician Reviewer, Branch 5

cc: