

Internal Revenue Service

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Person To Contact:
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Legend

Taxpayer =
Bank =
Subsidiary =
LLC =
Year 1 =
SCorp =
QSub 1 =
QSub 2 =
QSub 3 =

Dear :

This is in reply to a letter dated May 27, 2008, and additional information submitted by your authorized representative, requesting a ruling under § 1.1031(k) of the Income Tax Regulations. Specifically, the ruling you request is that a transfer of ownership of an entity that results in a change in the tax identity of the entity will not cause the entity to be considered a new qualified intermediary with respect to pending like-kind exchanges for purposes of § 1.1031(k).

Facts

Taxpayer is a calendar year financial holding company that uses the overall accrual method of accounting for its accounting books and records and for Federal income tax purposes. Taxpayer wholly owns Bank. Through its various subsidiaries and affiliates Taxpayer is a leader in investment banking, financial services for consumers, small business and commercial banking, financial transaction processing, asset management, and private equity.

Subsidiary is a wholly-owned corporate subsidiary of Bank. LLC is a single member limited liability company wholly owned by Bank. Primarily through the activities of Subsidiary and the subsidiaries of LLC, Bank is engaged in the business of serving as a qualified intermediary and as an exchange accommodation titleholder (EAT) pursuant to Rev. Proc. 2000-37, 2000-2 C.B. 308, for § 1031 like-kind exchanges.

In Year 1, Bank formed Subsidiary to purchase the assets of SCorp, an unrelated corporation taxed under Subchapter S of the Code. At the time of the Year 1 asset sale, SCorp, through three wholly-owned subsidiaries, acted as a qualified intermediary in large-volume, repetitive like-kind exchange programs (LKE Programs) that primarily involved exchanges of autos and trucks, each with volumes exceeding 100 transactions annually. The LKE Programs are intended to meet the requirements described in Rev. Proc. 2003-39, 2003-1 C.B. 971. The three wholly-owned subsidiaries, QSub 1, QSub 2 and QSub 3, are each disregarded for Federal income tax purposes as a qualified Subchapter S subsidiary (QSub) pursuant to §1362(b)(3)(A).

Bank intends to take direct ownership of the three QSubs, with the QSubs continuing to serve as qualified intermediaries in the LKE Programs subject to all contractual provisions relating to this function. This will be accomplished through a transfer of the stock of each QSub by SCorp to LLC for minimal consideration. Since LLC is not a qualified S corporation shareholder, each QSub will, after the stock transfer from SCorp to LLC, no longer be an eligible qualified S corporation subsidiary, convert to a C corporation, and no longer be disregarded for Federal income tax purposes. Consequently, there will be a change of the tax identity of the qualified intermediary for each LKE Program during the pendency of all exchanges commenced but not completed prior to the QSub stock transfer from SCorp to LLC.

Taxpayer represents that except for the change of ownership transaction, the QSubs and LLC have satisfied and will continue to satisfy all requirements provided in §1.1031(k)-1(g)(4) and Rev. Proc. 2003-39 to act as qualified intermediaries in the described LKE Programs. In addition, Taxpayer confirms that following the change of ownership of the QSubs leading to a change in their tax status, it does not intend to change the manner in which the QSubs conduct business or their forms of legal organization. Further, following the change of ownership, Subsidiary will continue to provide all personnel and administrative support required by the QSubs to provide services as qualified intermediaries pursuant to the management arrangements presently in place.

Law and Analysis

Section 1031(a)(1) provides that no gain or loss is recognized on an exchange of property held for productive use in a trade or business or for investment (relinquished

property) if the property is exchanged for property of like kind to be held either for productive use in a trade or business or for investment (replacement property). A taxpayer may engage in a deferred like-kind exchange under § 1031(a)(3). Section 1.1031(k)-1(a) defines a deferred exchange as an exchange in which, pursuant to an agreement, the taxpayer transfers relinquished property and subsequently receives replacement property. However, if a taxpayer actually or constructively receives money or other non-like-kind property before receiving like-kind replacement property, gain is recognized on the exchange. To assist taxpayers in structuring deferred exchange transactions in a way that avoids actual or constructive receipt of non-like-kind property, § 1.1031(k)-1(g) establishes safe harbors, including the allowance of a qualified intermediary (QI) to facilitate exchanges.

Section 1.1031(k)-1(g)(4)(iii)(B) provides, in part, that a QI is a person who enters into a written agreement with the taxpayer and, as required by the agreement, acquires the relinquished property from the taxpayer, transfers the relinquished property, acquires the replacement property, and transfers the replacement property to the taxpayer.

Solely for purposes of determining whether an intermediary is a QI under § 1.1031(k)-1(g)(4)(iii)(B), § 1.1031(k)-1(g)(4)(iv) provides that, regardless of whether an intermediary acquires and transfers property under general tax principles, an intermediary is treated as acquiring and transferring property if the intermediary acquires and transfers legal title to that property. In addition, an intermediary is treated as acquiring and transferring relinquished property if the intermediary enters into an agreement with a person other than the taxpayer for the transfer of the relinquished property to that person and, pursuant to that agreement, the relinquished property is transferred to that person. Similarly, an intermediary is treated as acquiring and transferring replacement property if the intermediary enters into an agreement with the owner of the replacement property for the transfer of that property and, pursuant to that agreement, the replacement property is transferred to the taxpayer.

Section 1.1031(k)-1(g)(4)(v) provides that, solely for purposes of §§ 1.1031(k)-1(g)(4)(iii) and (iv), an intermediary is treated as entering into an agreement to transfer property if the rights of a party to the agreement are assigned to the intermediary and all parties to that agreement are notified in writing of the assignment on or before the date the property is transferred.

Thus, under § 1.1031(k)-1(g), if a taxpayer uses a QI in a § 1031 exchange, the taxpayer is considered to have engaged in the exchange with the QI. Consequently, the QI considered the transferee of the relinquished property and the QI considered the transferor of the replacement property must be the same person or entity.

In the present situation, the transfer of ownership of QSub 1, QSub 2 and QSub 3 will result in a change in the tax identity of QSub 1, QSub 2 and QSub 3. Before the transfer, QSub 1, QSub 2 and QSub 3 were disregarded entities but after the transfer

they will be C corporations no longer disregarded for Federal income tax purposes. The legal identities of QSub 1, QSub 2 and QSub 3, however, will not change. QSub 1, QSub 2 and QSub 3 will, after their ownership transfer, each continue to be, for state law purposes, an entity engaged in the business of providing qualified intermediary services that is no different from the entity that existed prior to the transfer. With respect to pending like-kind exchanges (exchanges in which a taxpayer has transferred relinquished property to a QI but not yet received replacement property from the QI), a change from a disregarded entity to an entity no longer disregarded should not cause QSub 1, QSub 2 or QSub 3 to be treated as a QI that is different from the entity considered to be the transferee of the relinquished property.

Conclusion

Based on the facts and representations presented, conversion of the tax status of QSub 1, QSub 2 and QSub 3 from qualified S corporation subsidiaries into C corporations does not cause QSub 1, QSub 2 and QSub 3 to be treated as new or different QIs for purposes of the rules in § 1.1031(k)-1(g). Accordingly, with respect to pending like-kind exchanges, QSub 1, QSub 2 and QSub 3 will, after the ownership transfer, retain their status as the transferee of the relinquished property under § 1.1031(k)-1(g)(4)(iii)(B).

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Michael J. Montemurro
Branch Chief, Branch 4
(Income Tax & Accounting)