



transaction. Specifically, you have requested a ruling that the distribution from Trust to be made to Taxpayer of an undivided tenancy-in-common (“TIC”) interest in Property, subject to a binding contract for its disposition, as result of Trust’s involuntary termination, will not preclude such interest from being held for investment or for the productive use in a trade or business within the meaning of § 1031(a) of the Code.

## FACTS

Taxpayer is one of X beneficiaries of Trust, a testamentary trust whose terms were established by Decedent’s Will, dated Date 1, for the benefit of her Daughters and their descendants. Trust, created on Date 2, holds Property, real property located in State Z. Decedent’s Will provided for the Trust to cease upon the death of the last surviving child of Daughters who was living upon the death of Decedent (“Terminating Event”) and directed Trustees to distribute the Trust corpus to the beneficiaries in due course. Decedent’s Will granted Trustees broad powers to determine the nature of property and cash proceeds includible in any distributions and made those determinations binding on the beneficiaries. In addition, it did not provide the beneficiaries with the right to alienate his or her interest in the Trust.

During the period between Date 3 and Date 4, Trustees took no significant actions to dispose of the Property. After Date 4, Trustees, in their fiduciary duty to preserve the Trust corpus, determined that it would be in the best interests of the beneficiaries to engage in a like-kind exchange, under § 1031 of the Code, of the Property for other real properties and began negotiations with a potential buyer for its disposition. On Date 5, during the negotiations with the potential buyer, the Terminating Event occurred upon the death of Individual. After Date 5, Trustees completed negotiations and entered into a sales contract, subject to a due diligence clause, with the buyer to dispose of the Property (“Sales Contract”). At that time, Trustees also determined that it was no longer feasible for the Trust to consummate a § 1031 like-kind exchange of Property for other real properties because of the Terminating Event.

Trustees informed the beneficiaries of their intention to request for the State Z Probate Court (“Court”) to approve the disposition of Property as part of the overall approval of the termination plan for the Trust (“Termination Plan”).

Upon the Court’s approval, the Termination Plan will include the transactions described, in part, below. Trustees will finalize the Sales Contract to dispose of the Property with the buyer or another buyer in the unlikely event that the existing buyer terminates the Sales Contract after the due diligence period.

As part of the Termination Plan, Trustees agreed to accommodate any beneficiaries interested in completing exchanges in a manner like that which the Trustees initially contemplated prior to the Terminating Event. Y beneficiaries, including Taxpayer, informed Trustees of their desire to complete such an exchange (“Exchanging Beneficiary”).

Limited liability companies (hereinafter referred to as “LLC” or collectively as “LLCs”) will be formed and owned separately by each Exchanging Beneficiary, including Taxpayer. Each LLC will be disregarded as an entity separate from its sole member, within the meaning of § 301.7701-2(c)(2) and § 301.7701-3(b)(1)(ii) of the Procedure and Administration Regulations and will be managed initially by Trustees.

Following the creation of the LLCs, Trustees will make distributions of the appropriate undivided TIC interests in the Property, subject to the Sales Contract, to each Exchanging Beneficiary’s LLC. Shortly after the distributions, Trustees will cause the disposition of the TIC Interests. Each Exchanging Beneficiary, through his or her respective LLC, will engage in a separate exchange transaction.

Taxpayer also makes the following additional representations:

1. The Property has been held by the Trust for investment purposes throughout the Trust’s existence.
2. Any replacement properties acquired by Taxpayer through her LLC will be held for investment purposes.
3. The disposition of Taxpayer’s TIC Interest and the acquisition of replacement properties by Taxpayer through her respective LLC will be accomplished in a manner that in all respects, aside from the issue raised in this ruling, qualifies the transactions as a like-kind exchange eligible for nonrecognition treatment under § 1031 of the Code and the Income Tax Regulations thereunder.
4. Trust’s winding-up period, within the meaning of § 1.641(b)-3(b) of the Income Tax Regulations, has not been unduly postponed.

#### LAW AND ANALYSIS

Section 1031(a)(1) of the Code provides that no gain or loss shall 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 held either for productive use in a trade or business or for investment.

Section 1.1031(a)-1(b) of the Income Tax Regulations defines “like kind” as referring to the nature or character of the property and not to its grade or condition. The fact that the real estate involved in the exchange is improved or unimproved is not material, for that fact relates only to the grade or the quality of the property and not to its kind or class.

Section 1.641(b)-3(b) of the Income Tax Regulations generally provides that the determination of whether a trust has terminated depends upon whether the property held in trust has been distributed to the persons entitled to succeed to the property upon termination of the trust rather than upon the technicality of whether or not the trustee has rendered its final accounting. A trust does not automatically terminate upon the

happening of the event by which the duration of the trust is measured. A reasonable time is permitted after such event for the trustee to perform the duties necessary to complete the administration of the trust. However, the trust's winding-up period cannot be unduly postponed and if the distribution of the trust corpus is unreasonably delayed, the trust will be considered as terminated for federal income tax purposes after the expiration of a reasonable period for the trustee to complete the administration of the trust.

Under § 301.7701-3(b)(1)(ii) of the Procedure and Administration Regulations, 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) of the Procedure and Administration Regulations, 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 Rev. Rul. 75-292, 1975-2 C.B. 333, an individual taxpayer, in a prearranged transaction, transferred land and buildings used in the taxpayer's trade or business to an unrelated corporation in exchange for land and an office building owned by the corporation and used in its trade or business. Immediately following the exchange, the individual taxpayer transferred the newly acquired land and office building to the individual's newly created corporation in exchange for stock in the same corporation in a transaction that qualified for nonrecognition of gain under § 351. The revenue ruling concluded that the individual 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 by that taxpayer but that the taxpayer acquired the replacement property for the purpose of transferring it to the new corporation. As a result, the exchange did not qualify for nonrecognition under § 1031.

In Rev. Rul. 77-337, 1977-2 C.B. 305, an individual taxpayer, in a prearranged plan, liquidated all the stock of a corporation and transferred the corporation's sole asset, a shopping center, to a third party in exchange for like-kind property. Rev. Rul. 77-337 noted that under Rev. Rul. 75-292, a newly created corporation's eventual productive use of property in its trade or business is not attributable to its sole shareholder. Consequently, the individual taxpayer did not hold the shopping center for use in a trade or business or for investment, because the corporation's previous trade or business use could not be attributed to its sole shareholder. Thus, the exchange did not qualify for nonrecognition of gain or loss under § 1031.

Section 1031 of the Code includes a "holding" requirement that requires both the relinquished property and the replacement property to be held for productive use in a trade or business or held for investment. This provision was designed, in part, to postpone the recognition of gain or loss when property used in a trade or business or held for investment is exchanged for other property in the course of the continuing

operation of that trade or business, or in the course of investment. Under these circumstances, a taxpayer is not considered to have received a gain nor suffered a loss in a general and economic sense, nor has the exchange of property resulted in the termination of one venture and an assumption of a new venture. The business venture operated before the exchange continues after the exchange without any real economic change or alteration, and without the realization of any cash or readily liquefiable assets. See Carlton v. United States, 385 F.2d 238 (5<sup>th</sup> Cir. 1967); Jordan Marsh Co. v. Comm'r, 269 F.2d 453 (2<sup>nd</sup> Cir. 1959); cf. Portland Oil Co. v. Comm'r, 109 F.2d 479 (1<sup>st</sup> Cir. 1940). See generally § 1.1002-1(c) (“[t]he underlying assumption of these exceptions [e.g., § 1031] is that the new property is substantially a continuation of the old investment still unliquidated”).

In this case, the Terminating Event, as defined by the terms of Trust’s governing instrument, occurred after many years of the Trust’s existence. Because the Trust was a testamentary trust, the Terminating Event was fixed by the Decedent and could not be modified or changed.

Based on the representation that Taxpayer’s LLC will be disregarded as an entity separate from Taxpayer, the distribution of the TIC Interest by Trust to the LLC will be considered, for federal income tax purposes, as a distribution of the TIC interest to Taxpayer. The Termination Plan is anticipated to be approved by the State Z Probate Court and implemented as described above without regard to whether the exchange of Taxpayer’s TIC Interest for eligible like-kind replacement property is consummated (“Proposed Exchange”). Accordingly, Trust’s distribution of Taxpayer’s TIC Interest, pursuant to the Termination Plan, will be wholly independent of Taxpayer’s Proposed Exchange. The facts herein are distinguishable from those in Rev. Rul. 75-292 and Rev. Rul. 77-337, which involve voluntary transfers of properties pursuant to prearranged plans.

Based on the authorities discussed above and the facts and representations submitted by Taxpayer, we rule that the distribution from Trust to be made to Taxpayer of the TIC Interest, subject to the Sales Contract, as result of Trust’s involuntary termination, will not preclude such Interest from being held for investment or for the productive use in a trade or business within the meaning of § 1031(a) of the Code.

This ruling is based upon facts and representations submitted by Taxpayer and accompanied by a penalty-of-perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the request for a ruling. However, as part of an examination process, the Service may verify the factual information, representations, and other data submitted. No determination is made by this ruling letter as to whether the described transaction otherwise qualifies for deferral of gain realized under § 1031 of the Code. We have no opinion, express nor implied, except as specifically ruled above, as to the federal income 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. Nor 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. Further, no determination is made by this ruling letter as to whether the Trust remains in existence within the meaning of § 1.641(b)-3(b) of the Income Tax Regulations.

A copy of this ruling letter should be attached to any income tax return to which it is relevant.

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

This letter ruling is being issued electronically in accordance with Rev. Proc. 2023-1, 2023-1 I.R.B. 1. A paper copy will not be mailed to Taxpayer.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to Taxpayer's authorized representatives.

Sincerely,

Alexa T. Dubert  
Senior Technician Reviewer  
Branch 4  
Office of Associate Chief Counsel  
(Income Tax & Accounting)

cc: