

## TITLE 26 -- INTERNAL REVENUE SERVICE REGULATIONS

### CHAPTER I -- INTERNAL REVENUE SERVICE DEPARTMENT OF THE TREASURY

#### SUBCHAPTER A -- INCOME TAX

#### PART 1 -- INCOME TAXES

#### NORMAL TAXES AND SURTAXES

#### GAIN OR LOSS ON DISPOSITION OF PROPERTY

#### COMMON NONTAXABLE EXCHANGES

### Section 1.1031-0 – Index

§ 1.1031-0	Index
§ 1.1031 (a)-1	Property held for productive use in a trade or business or for investment
§ 1.1031 (a)-1(a)	In general
§ 1.1031 (a)-1(a)(1)	Exchanges of property solely for property of a like kind
§ 1.1031 (a)-1(a)(2)	Exchanges of property not solely for property of a like kind
§ 1.1031 (a)-1(b)	Definition of like kind
§ 1.1031 (a)-1(c)	Examples of exchanges of property of a "like kind"
§ 1.1031 (a)-1(d)	Examples of exchanges not solely in kind
§ 1.1031 (a)-1(e)	Effective date
§ 1.1031(a)-2	Additional rules for exchanges of personal property
§ 1.1031 (a)-2(a)	Introduction
§ 1.1031 (a)-2(b)	Depreciable tangible personal property



# EXETER

1031 Exchange Services LLC

- § 1.1031 (a)-2(b)(1) General Rule
- § 1.1031 (a)-2(b)(2) General Asset Classes
- § 1.1031 (a)-2(b)(3) Product Classes
- § 1.1031 (a)-2(b)(4) Modifications of NAICS product classes
- § 1.1031 (a)-2(b)(5) Administrative procedures for revising general asset classes
- § 1.1031 (a)-2(c) Intangible personal property and nondepreciable personal property
- § 1.1031 (a)-2(d) Effective Date
- § 1.1031 (b)-1 Receipt of other property or money in tax-free exchange
- § 1.1031 (b)-2 Safe harbor for Qualified Intermediaries (“Accommodators”)
- § 1.1031 (c)-1 Nonrecognition of loss
- § 1.1031 (d)-1 Property acquired upon a tax-free exchange.
- § 1.1031 (d)-1T Coordination of section 1060 with section 1031 (temporary)
- § 1.1031 (d)-2 Treatment of assumption of liabilities
- § 1.1031 (e)-1 Exchanges of livestock of different sexes
- § 1.1031 (j)-1 Exchanges of multiple properties
- § 1.1031 (j)-1(a) Introduction
- § 1.1031 (j)-1(b) Computation of gain recognized
- § 1.1031 (j)-1(c) Computation of basis of properties received
- § 1.1031 (j)-1(d) Examples
- § 1.1031 (j)-1(e) Effective date
- § 1.1031 (k)-1 Treatment of deferred exchanges
- § 1.1031 (k)-1(a) Overview
- § 1.1031 (k)-1(b) Identification and receipt requirements
- § 1.1031 (k)-1(c) Identification of replacement property before end of identification



# EXETER

1031 Exchange Services LLC

period

- § 1.1031 (k)-1(d) Receipt of identified replacement property
- § 1.1031 (k)-1(e) Special rules for identification and receipt of replacement property to be produced.
- § 1.1031 (k)-1(f) Receipt of money or other property
- § 1.1031 (k)-1(g) Safe harbors
- § 1.1031 (k)-1(h) Interest and growth factors
- § 1.1031 (k)-1(i) [Reserved]
- § 1.1031 (k)-1(j) Determination of gain or loss recognized and the basis of property received in a deferred exchange
- § 1.1031 (k)-1(k) Definition of disqualified person
- § 1.1031 (k)-1(l) [Reserved]
- § 1.1031 (k)-1(m) Definition of fair market value
- § 1.1031 (k)-1(n) No inference with respect to actual or constructive receipt rules outside of section 1031.
- § 1.1031 (k)-1(o) Effective date.

END OF INDEX



# EXETER

1031 Exchange Services LLC

1 § 1.1031(a)-1 Property held for productive use in a trade or business or for investment.

2

3 (a) In general—

4

5 (1) Exchanges of property solely for property of a like kind.

6

7 Section 1031(a)(1) provides an exception from the general rule requiring the  
8 recognition of gain or loss upon the sale or exchange of property. Under section  
9 1031(a)(1), no gain or loss is recognized if property held for productive use in a trade  
10 or business or for investment is exchanged solely for property of a like kind to be held  
11 either for productive use in a trade or business or for investment. Under section  
12 1031(a)(1), property held for productive use in a trade or business may be exchanged  
13 for property held for investment. Similarly, under section 1031(a)(1), property held for  
14 investment may be exchanged for property held for productive use in a trade or  
15 business. However, section 1031(a)(2) provides that section 1031(a)(1) does not apply  
16 to any exchange of--

17

18 (i) Stock in trade or other property held primarily for sale;

19

20 (ii) Stocks, bonds, or notes;

21

22 (iii) Other securities or evidences of indebtedness or interest;

23

24 (iv) Interests in a partnership;

25

26 (v) Certificates of trust or beneficial interests; or

27

28 (vi) Choses in action.

29

30 Section 1031(a)(1) does not apply to any exchange of interests in a partnership  
31 regardless of whether the interests exchanged are general or limited partnership  
32 interests or are interests in the same partnership or in different partnerships. An  
33 interest in a partnership that has in effect a valid election under section 761(a) to be  
34 excluded from the application of all of subchapter K is treated as an interest in each of  
35 the assets of the partnership and not as an interest in a partnership for purposes of  
36 section 1031(a)(2)(D) and paragraph (a)(1)(iv) of this section. An exchange of an  
37 interest in such a partnership does not qualify for nonrecognition of gain or loss under  
38 section 1031 with respect to any asset of the partnership that is described in section  
39 1031(a)(2) or to the extent the exchange of assets of the partnership does not  
40 otherwise satisfy the requirements of section 1031(a).

41

42 (2) Exchanges of property not solely for property of a like kind.

43

44 A transfer is not within the provisions of section 1031(a) if, as part of the  
45 consideration, the taxpayer receives money or property which does not meet the  
46 requirements of section 1031(a), but the transfer, if otherwise qualified, will be within  
47 the provisions of either section 1031 (b) or (c). Similarly, a transfer is not within the



# EXETER

1031 Exchange Services LLC

1 provisions of section 1031(a) if, as part of the consideration, the other party to the  
2 exchange assumes a liability of the taxpayer (or acquires property from the taxpayer  
3 that is subject to a liability), but the transfer, if otherwise qualified, will be within the  
4 provisions of either section 1031 (b) or (c). A transfer of property meeting the  
5 requirements of section 1031(a) may be within the provisions of section 1031(a) even  
6 though the taxpayer transfers in addition property not meeting the requirements of  
7 section 1031(a) or money. However, the nonrecognition treatment provided by section  
8 1031(a) does not apply to the property transferred which does not meet the  
9 requirements of section 1031(a).

10  
11 (b) Definition of "like kind."

12  
13 As used in section 1031(a), the words like kind have reference to the nature or  
14 character of the property and not to its grade or quality. One kind or class of property  
15 may not, under that section, be exchanged for property of a different kind or class. The  
16 fact that any real estate involved is improved or unimproved is not material, for that  
17 fact relates only to the grade or quality of the property and not to its kind or class.  
18 Unproductive real estate held by one other than a dealer for future use or future  
19 realization of the increment in value is held for investment and not primarily for sale.  
20 For additional rules for exchanges of personal property, see § 1.1031 (a)-2.

21  
22 (c) Examples of exchanges of property of a "like kind."

23  
24 No gain or loss is recognized if (1) a taxpayer exchanges property held for productive  
25 use in his trade or business, together with cash, for other property of like kind for the  
26 same use, such as a truck for a new truck or a passenger automobile for a new  
27 passenger automobile to be used for a like purpose; or (2) a taxpayer who is not a  
28 dealer in real estate exchanges city real estate for a ranch or farm, or exchanges a  
29 leasehold of a fee with 30 years or more to run for real estate, or exchanges improved  
30 real estate for unimproved real estate; or (3) a taxpayer exchanges investment property  
31 and cash for investment property of a like kind.

32  
33 (d) Examples of exchanges not solely in kind.

34  
35 Gain or loss is recognized if, for instance, a taxpayer exchanges (1) Treasury bonds  
36 maturing March 15, 1958, for Treasury bonds maturing December 15, 1968, unless  
37 section 1037(a) (or so much of section 1031 as relates to section 1037(a)) applies to  
38 such exchange, or (2) a real estate mortgage for consolidated farm loan bonds.

39  
40 (e) Effective date relating to exchanges of partnership interests.

41  
42 The provisions of paragraph (a)(1) of this section relating to exchanges of partnership  
43 interests apply to transfers of property made by taxpayers on or after April 25, 1991.

44  
45 § 1.1031(a)-2 Additional rules for exchanges of personal property.

46  
47 (a) Introduction.



# EXETER

1031 Exchange Services LLC

1  
2 Section 1.1031(a)-1(b) provides that the nonrecognition rules of section 1031 do not  
3 apply to an exchange of one kind or class of property for property of a different kind or  
4 class. This section contains additional rules for determining whether personal property  
5 has been exchanged for property of a like kind or like class. Personal properties of a  
6 like class are considered to be of a "like kind" for purposes of section 1031. In  
7 addition, an exchange of properties of a like kind may qualify under section 1031  
8 regardless of whether the properties are also of a like class. In determining whether  
9 exchanged properties are of a like kind, no inference is to be drawn from the fact that  
10 the properties are not of a like class. Under paragraph (b) of this section, depreciable  
11 tangible personal properties are of a like class if they are either within the same  
12 General Asset Class (as defined in paragraph (b)(2) of this section) or within the same  
13 Product Class (as defined in paragraph (b)(3) of this section). Paragraph (c) of this  
14 section provides rules for exchanges of intangible personal property and  
15 nondepreciable personal property.

16  
17 (b) Depreciable tangible personal property –

18  
19 (1) General rule.

20  
21 Depreciable tangible personal property is exchanged for property of a "like kind" under  
22 section 1031 if the property is exchanged for property of a like kind or like class.  
23 Depreciable tangible personal property is of a like class to other depreciable tangible  
24 personal property if the exchanged properties are either within the same General Asset  
25 Class or within the same Product Class. A single property may not be classified within  
26 more than one General Asset Class or within more than one Product Class. In  
27 addition, property classified within any General Asset Class may not be classified  
28 within a Product Class. A property's General Asset Class or Product Class is  
29 determined as of the date of the exchange.

30  
31 (2) General Asset Classes.

32  
33 Except as provided in paragraphs (b)(4) and (b)(5) of this section, property within a  
34 General Asset Class consists of depreciable tangible personal property described in  
35 one of asset classes 00.11 through 00.28 and 00.4 of Rev. Proc. 87-56, 1987-2 C.B.  
36 674. These General Asset Classes describe types of depreciable tangible personal  
37 property that frequently are used in many businesses.

38  
39 The General Asset Classes are as follows:

- 40  
41 (i) Office furniture, fixtures, and equipment (asset class 00.11),  
42  
43 (ii) Information systems (computers and peripheral equipment) (asset class 00.12),  
44  
45 (iii) Data handling equipment, except computers (asset class 00.13),  
46  
47 (iv) Airplanes (airframes and engines), except those used in commercial or contract



# EXETER

1031 Exchange Services LLC

1 carrying of passengers or freight, and all helicopters (airframes and engines) (asset  
2 class 00.21),  
3

4 (v) Automobiles, taxis (asset class 00.22),  
5

6 (vi) Buses (asset class 00.23),  
7

8 (vii) Light general purpose trucks (asset class 00.241),  
9

10 (viii) Heavy general purpose trucks (asset class 00.242),  
11

12 (ix) Railroad cars and locomotives, except those owned by railroad transportation  
13 companies (asset class 00.25),  
14

15 (x) Tractor units for use over-the-road (asset class 00.26),  
16

17 (xi) Trailers and trailer-mounted containers (asset class 00.27),  
18

19 (xii) Vessels, barges, tugs, and similar water-transportation equipment, except those  
20 used in marine construction (asset class 00.28), and  
21

22 (xiii) Industrial steam and electric generation and/or distribution systems (asset class  
23 00.4).  
24

25 (3) Product classes.  
26

27 Except as provided in paragraphs (b)(4) and (5) of this section, or as provided by the  
28 Commissioner in published guidance of general applicability, property within a  
29 product class consists of depreciable tangible personal property that is described in a  
30 6-digit product class within Sectors 31, 32, and 33 (pertaining to manufacturing  
31 industries) of the North American Industry Classification System (NAICS), set forth in  
32 Executive Office of the President, Office of Management and Budget, North American  
33 Industry Classification System, United States, 2002 (NAICS Manual), as periodically  
34 updated. Copies of the NAICS Manual may be obtained from the National Technical  
35 Information Service, an agency of the U.S. Department of Commerce, and may be  
36 accessed on the internet. Sectors 31 through 33 of the NAICS Manual contain listings  
37 of specialized industries for the manufacture of described products and equipment.  
38 For this purpose, any 6-digit NAICS product class with a last digit of 9 (a  
39 miscellaneous category) is not a product class for purposes of this section. If a  
40 property is listed in more than one product class, the property is treated as listed in  
41 any one of those product classes. A property's 6-digit product class is referred to as  
42 the property's NAICS code.  
43

44 (4) Modifications of NAICS product classes.  
45

46 The product classes of the NAICS Manual may be updated or otherwise modified from  
47 time to time as the manual is updated, effective on or after the date of the





# EXETER

1031 Exchange Services LLC

1 modification. The NAICS Manual generally is modified every five years, in years ending  
2 in a 2 or 7 (such as 2002, 2007, and 2012). The applicability date of the modified  
3 NAICS Manual is announced in the Federal Register and generally is January 1 of the  
4 year the NAICS Manual is modified. Taxpayers may rely on these modifications as they  
5 become effective in structuring exchanges under this section. Taxpayers may rely on  
6 the previous NAICS Manual for transfers of property made by a taxpayer during the  
7 one-year period following the effective date of the modification. For transfers of  
8 property made by a taxpayer on or after January 1, 1997, and on or before January 1,  
9 2003, the NAICS Manual of 1997 may be used for determining product classes of the  
10 exchanged property.

11  
12 (5) Administrative procedures for revising general asset classes and product classes.

13  
14 The Commissioner may, through published guidance of general applicability,  
15 supplement, modify, clarify, or update the guidance relating to the classification of  
16 properties provided in this paragraph (b). (See § 601.601(d)(2) of this chapter.) For  
17 example, the Commissioner may determine not to follow (in whole or in part) a general  
18 asset class for purposes of identifying property of like class, may determine not to  
19 follow (in whole or in part) any modification of product classes published in the NAICS  
20 Manual, or may determine that other properties not listed within the same or in any  
21 product class or general asset class nevertheless are of a like class. The Commissioner  
22 also may determine that two items of property that are listed in separate product  
23 classes or in product classes with a last digit of 9 are of a like class, or that an item of  
24 property that has a NAICS code is of a like class to an item of property that does not  
25 have a NAICS code.

26  
27 (6) No inference outside of section 1031.

28  
29 The rules provided in this section concerning the use of general asset classes or  
30 product classes are limited to exchanges under section 1031. No inference is intended  
31 with respect to the classification of property for other purposes, such as depreciation.

32  
33 (7) Examples.

34  
35 The application of this paragraph (b) may be illustrated by the following examples:

36  
37 Example 1. Taxpayer A transfers a personal computer (asset class 00.12) to B in  
38 exchange for a printer (asset class 00.12). With respect to A, the properties exchanged  
39 are within the same General Asset Class and therefore are of a like class.

40  
41 Example 2. Taxpayer C transfers an airplane (asset class 00.21) to D in exchange for a  
42 heavy general purpose truck (asset class 00.242). The properties exchanged are not of  
43 a like class because they are within different General Asset Classes. Because each of  
44 the properties is within a General Asset Class, the properties may not be classified  
45 within a Product Class. The airplane and heavy general purpose truck are also not of a  
46 like kind. Therefore, the exchange does not qualify for nonrecognition of gain or loss  
47 under section 1031.





# EXETER

1031 Exchange Services LLC

1  
2 Example 3. Taxpayer E transfers a grader to F in exchange for a scraper. Neither  
3 property is within any of the general asset classes. However, both properties are within  
4 the same product class (NAICS code 333120). The grader and scraper are of a like  
5 class and deemed to be of a like kind for purposes of section 1031.

6  
7 Example 4. Taxpayer G transfers a personal computer (asset class 00.12), an airplane  
8 (asset class 00.21) and a sanding machine (NAICS code 333210), to H in exchange for  
9 a printer (asset class 00.12), a heavy general purpose truck (asset class 00.242) and a  
10 lathe (NAICS code 333210). The personal computer and the printer are of a like class  
11 because they are within the same general asset class. The sanding machine and the  
12 lathe are of a like class because they are within the same product class (although  
13 neither property is within any of the general asset classes). The airplane and the heavy  
14 general purpose truck are neither within the same general asset class nor within the  
15 same product class, and are not of a like kind.

16  
17 (8) Transition rule.

18  
19 Properties within the same product classes based on the 4-digit codes contained in  
20 Division D of the Executive Office of the President, Office of Management and Budget,  
21 Standard Industrial Classification Manual (1987), will be treated as property of a like  
22 class for transfers of property made by taxpayers on or before May 19, 2005.

23  
24 (c) Intangible personal property and nondepreciable personal property –

25  
26 (1) General rule.

27  
28 An exchange of intangible personal property of nondepreciable personal property  
29 qualifies for nonrecognition of gain or loss under section 1031 only if the exchanged  
30 properties are of a like kind. No like classes are provided for these properties. Whether  
31 intangible personal property is of a like kind to other intangible personal property  
32 generally depends on the nature or character of the rights involved (e.g., a patent or a  
33 copyright) and also on the nature or character of the underlying property to which the  
34 intangible personal property relates.

35  
36 (2) Goodwill and going concern value.

37  
38 The goodwill or going concern value of a business is not of a like kind to the goodwill  
39 or going concern value of another business.

40  
41 (3) Examples.

42  
43 The application of this paragraph (c) may be illustrated by the following examples:

44  
45 Example (1). Taxpayer K exchanges a copyright on a novel for a copyright on a  
46 different novel. The properties exchanged are of a like kind.

47



# EXETER

1031 Exchange Services LLC

1 Example (2). Taxpayer J exchanges a copyright on a novel for a copyright on a song.  
2 The properties exchanged are not of a like kind.

3  
4 (d) Effective date.

5  
6 Except as otherwise provided in this paragraph (d), this section applies to exchanges  
7 occurring on or after April 11, 1991. Paragraphs (b)(3) through (b)(6), Example 3 and  
8 Example 4 of paragraph (b)(7), and paragraph (b)(8) of this section apply to transfers of  
9 property made by taxpayers on or after August 12, 2004. However, taxpayers may  
10 apply paragraphs (b)(3) through (b)(6), and Example 3 and Example 4 of paragraph  
11 (b)(7) of this section to transfers of property made by taxpayers on or after January 1,  
12 1997, in taxable years for which the period of limitation for filing a claim for refund or  
13 credit under section 6511 has not expired.

14  
15 § 1.1031(b)-1 Receipt of other property or money in tax-free exchange

16  
17 (a) If the taxpayer receives other property (in addition to property permitted to be  
18 received without recognition of gain) or money--

19  
20 (1) In an exchange described in section 1031(a) of property held for investment or  
21 productive use in trade or business for property of like kind to be held either for  
22 productive use or for investment,

23  
24 (2) In an exchange described in section 1035(a) of insurance policies or annuity  
25 contracts,

26  
27 (3) In an exchange described in section 1036(a) of common stock for common stock, or  
28 preferred stock for preferred stock, in the same corporation and not in connection with  
29 a corporate reorganization, or

30  
31 (4) In an exchange described in section 1037(a) of obligations of the United States,  
32 issued under the Second Liberty Bond Act (31 U.S.C. 774 (2)), solely for other  
33 obligations issued under such Act, the gain, if any, to the taxpayer will be recognized  
34 under section 1031(b) in an amount not in excess of the sum of the money and the fair  
35 market value of the other property, but the loss, if any, to the taxpayer from such an  
36 exchange will not be recognized under section 1031(c) to any extent.

37  
38 (b) The application of this section may be illustrated by the following examples:

39  
40 Example 1. A, who is not a dealer in real estate, in 1954 exchanges real estate held for  
41 investment, which he purchased in 1940 for \$ 5,000, for other real estate (to be held  
42 for productive use in trade or business) which has a fair market value of \$ 6,000, and  
43 \$ 2,000 in cash. The gain from the transaction is \$ 3,000, but is recognized only to the  
44 extent of the cash received of \$ 2,000.

45  
46 Example 2. (a) B, who uses the cash receipts and disbursements method of accounting  
47 and the calendar year as his taxable year, has never elected under section 454(a) to



# EXETER

1031 Exchange Services LLC

1 include in gross income currently the annual increase in the redemption price of non-  
2 interest-bearing obligations issued at a discount. In 1943, for \$ 750 each, B  
3 purchased four \$ 1,000 series E U.S. savings bonds bearing an issue date of March 1,  
4 1943.

5

6 (b) On October 1, 1963, the redemption value of each such bond was \$ 1,396, and the  
7 total redemption value of the four bonds was \$ 5,584. On that date B submitted the  
8 four \$ 1,000 series E bonds to the United States in a transaction in which one of such  
9 \$ 1,000 bonds was reissued by issuing four \$ 100 series E U.S. savings bonds bearing  
10 an issue date of March 1, 1943, and by considering six \$ 100 series E bonds bearing  
11 an issue date of March 1, 1943, to have been issued. The redemption value of each  
12 such \$ 100 series E bond was \$ 139.60 on October 1, 1963. Then, as part of the  
13 transaction, the six \$ 100 series E bonds so considered to have been issued and the  
14 three \$ 1,000 series E bonds were exchanged, in an exchange qualifying under section  
15 1037(a), for five \$ 1,000 series H U.S. savings bonds plus \$ 25.60 in cash.

16

17 (c) The gain realized on the exchange qualifying under section 1037(a) is \$ 2,325.60,  
18 determined as follows:

Amount realized:

Par value of five series H bonds	\$ 5,000.00	
Cash received	25.60	-----
Total realized	5,025.60	
Less: Adjusted basis of series E bonds surrendered in the exchange:		
Three \$1,000 series E bonds	\$ 2,250.00	
Six \$100 series E bonds at \$75 each	450.00	
		2,700.00
Gain realized	-----	2,325.60

19  
20

21 (d) Pursuant to section 1031(b), only \$ 25.60 (the money received) of the total gain of \$  
22 2,325.60 realized on the exchange is recognized at the time of exchange and must be  
23 included in B's gross income for 1963. The \$ 2,300 balance of the gain (\$ 2,325.60  
24 less \$ 25.60) must be included in B's gross income for the taxable year in which the  
25 series H bonds are redeemed or disposed of, or reach final maturity, whichever is  
26 earlier, as provided in paragraph (c) of § 1.454-1.

27

28 (e) The gain on the four \$ 100 series E bonds, determined by using \$ 75 as a basis for  
29 each such bond, must be included in B's gross income for the taxable year in which  
30 such bonds are redeemed or disposed of, or reach final maturity, whichever is earlier.

31

32 Example 3. (a) The facts are the same as in example (2), except that, as part of the



# EXETER

1031 Exchange Services LLC

1 transaction, the \$ 1,000 series E bond is reissued by considering ten \$ 100 series E  
2 bonds bearing an issue date of March 1, 1943, to have been issued. Six of the \$ 100  
3 series E bonds so considered to have been issued are surrendered to the United States  
4 as part of the exchange qualifying under section 1037(a) and the other four are  
5 immediately redeemed.

6  
7 (b) Pursuant to section 1031(b), only \$ 25.60 (the money received) of the total gain of \$  
8 2,325.60 realized on the exchange qualifying under section 1037(a) is recognized at  
9 the time of the exchange and must be included in B's gross income for 1963. The \$  
10 2,300 balance of the gain (\$ 2,325.60 less \$ 25.60) realized on such exchange must be  
11 included in B's gross income for the taxable year in which the series H bonds are  
12 redeemed or disposed of, or reach final maturity, whichever is earlier, as provided in  
13 paragraph (c) of § 1.454-1.

14  
15 (c) The redemption on October 1, 1963, of the four \$ 100 series E bonds considered to  
16 have been issued at such time results in gain of \$ 258.40, which is then recognized  
17 and must be included in B's gross income for 1963. This gain of \$ 258.40 is the  
18 difference between the \$ 558.40 redemption value of such bonds on the date of the  
19 exchange and the \$ 300 (4 x \$ 75) paid for such series E bonds in 1943.

20  
21 Example 4. On November 1, 1963, C purchased for \$ 91 a marketable U.S. bond  
22 which was originally issued at its par value of \$ 100 under the Second Liberty Bond  
23 Act. On February 1, 1964, in an exchange qualifying under section 1037(a), C  
24 surrendered the bond to the United States for another marketable U.S. bond, which  
25 then had a fair market value of \$ 92, and \$ 1.85 in cash, \$ 0.85 of which was interest.  
26 The \$ 0.85 interest received is includible in gross income for the taxable year of the  
27 exchange, but the \$ 2 gain (\$ 93 less \$ 91) realized on the exchange is recognized for  
28 such year under section 1031(b) to the extent of \$ 1 (the money received). Under  
29 section 1031(d), C's basis in the bond received in exchange is \$ 91 (his basis of \$ 91 in  
30 the bond surrendered, reduced by the \$ 1 money received and increased by the \$ 1  
31 gain recognized).

32  
33 (c) Consideration received in the form of an assumption of liabilities (or a transfer  
34 subject to a liability) is to be treated as other property or money for the purposes of  
35 section 1031(b). Where, on an exchange described in section 1031(b), each party to the  
36 exchange either assumes a liability of the other party or acquires property subject to a  
37 liability, then, in determining the amount of other property or money for purposes of  
38 section 1031(b), consideration given in the form of an assumption of liabilities (or a  
39 receipt of property subject to a liability) shall be offset against consideration received  
40 in the form of an assumption of liabilities (or a transfer subject to a liability). See §  
41 1.1031(d)-2, examples (1) and (2).

42  
43 § 1.1031(b)-2 Safe harbor for Qualified Intermediaries ("Accommodator")

44  
45 (a) In the case of simultaneous transfers of like-kind properties involving a qualified  
46 intermediary (as defined in § 1.1031(k)-1(g)(4)(iii)), the qualified intermediary is not  
47 considered the agent of the taxpayer for purposes of section 1031(a). In such a case,



# EXETER

1031 Exchange Services LLC

1 the transfer and receipt of property by the taxpayer is treated as an exchange.

2  
3 (b) In the case of simultaneous exchanges of like-kind properties involving a qualified  
4 intermediary (as defined in § 1.1031(k)-1(g)(4)(iii)), the receipt by the taxpayer of an  
5 evidence of indebtedness of the transferee of the qualified intermediary is treated as  
6 the receipt of an evidence of indebtedness of the person acquiring property from the  
7 taxpayer for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter.

8  
9 (c) Paragraph (a) of this section applies to transfers of property made by taxpayers on  
10 or after June 10, 1991.

11  
12 (d) Paragraph (b) of this section applies to transfers of property made by taxpayers on  
13 or after April 20, 1994. A taxpayer may choose to apply paragraph (b) of this section to  
14 transfers of property made on or after June 10, 1991.

15  
16 § 1.1031(c)-1 Nonrecognition of loss.

17  
18 Section 1031(c) provides that a loss shall not be recognized from an exchange of  
19 property described in section 1031(a), 1035(a), 1036(a), or 1037(a) where there is  
20 received in the exchange other property or money in addition to property permitted to  
21 be received without recognition of gain or loss. See example (4) of paragraph (a)(3) of §  
22 1.1037-1 for an illustration of the application of this section in the case of an  
23 exchange of U.S. obligations described in section 1037(a).

24  
25 § 1.1031(d)-1 Property acquired upon a tax-free exchange.

26  
27 (a) If, in an exchange of property solely of the type described in section 1031, section  
28 1035(a), section 1036(a), or section 1037(a), no part of the gain or loss was recognized  
29 under the law applicable to the year in which the exchange was made, the basis of the  
30 property acquired is the same as the basis of the property transferred by the taxpayer  
31 with proper adjustments to the date of the exchange. If additional consideration is  
32 given by the taxpayer in the exchange, the basis of the property acquired shall be the  
33 same as the property transferred increased by the amount of additional consideration  
34 given (see section 1016 and the regulations thereunder).

35  
36 (b) If, in an exchange of properties of the type indicated in section 1031, section  
37 1035(a), section 1036(a), or section 1037(a), gain to the taxpayer was recognized under  
38 the provisions of section 1031(b) or a similar provision of a prior revenue law, on  
39 account of the receipt of money in the transaction, the basis of the property acquired  
40 is the basis of the property transferred (adjusted to the date of the exchange),  
41 decreased by the amount of money received and increased by the amount of gain  
42 recognized on the exchange. The application of this paragraph may be illustrated by  
43 the following example:

44  
45 Example. A, an individual in the moving and storage business, in 1954 transfers one  
46 of his moving trucks with an adjusted basis in his hands of \$ 2,500 to B in exchange  
47 for a truck (to be used in A's business) with a fair market value of \$ 2,400 and \$ 200



# EXETER

1031 Exchange Services LLC

1 in cash. A realizes a gain of \$ 100 upon the exchange, all of which is recognized under  
2 section 1031(b). The basis of the truck acquired by A is determined as follows:

Adjusted basis of A's former truck	\$ 2,500
Less: Amount of money received	200
	-----
Difference	2,300
Plus: Amount of gain recognized	100
	-----
Basis of truck acquired by A	2,400

3  
4 (c) If, upon an exchange of properties of the type described in section 1031, section  
5 1035(a), section 1036(a), or section 1037(a), the taxpayer received other property (not  
6 permitted to be received without the recognition of gain) and gain from the transaction  
7 was recognized as required under section 1031(b), or a similar provision of a prior  
8 revenue law, the basis (adjusted to the date of the exchange) of the property  
9 transferred by the taxpayer, decreased by the amount of any money received and  
10 increased by the amount of gain recognized, must be allocated to and is the basis of  
11 the properties (other than money) received on the exchange. For the purpose of the  
12 allocation of the basis of the properties received, there must be assigned to such other  
13 property an amount equivalent to its fair market value at the date of the exchange.

14  
15 The application of this paragraph may be illustrated by the following example:

16  
17 Example. A, who is not a dealer in real estate, in 1954 transfers real estate held for  
18 investment which he purchased in 1940 for \$ 10,000 in exchange for other real estate  
19 (to be held for investment) which has a fair market value of \$ 9,000, an automobile  
20 which has a fair market value of \$ 2,000, and \$ 1,500 in cash. A realizes a gain of \$  
21 2,500, all of which is recognized under section 1031(b). The basis of the property  
22 received in exchange is the basis of the real estate A transfers (\$ 10,000) decreased by  
23 the amount of money received (\$ 1,500) and increased in the amount of gain that was  
24 recognized (\$ 2,500), which results in a basis for the property received of \$ 11,000.  
25 This basis of \$11,000 is allocated between the automobile and the real estate received  
26 by A, the basis of the automobile being its fair market value at the date of the  
27 exchange, \$2,000, and the basis of the real estate received being the remainder,  
28 \$9,000.

29  
30 (d) Section 1031(c) and, with respect to section 1031 and section 1036(a), similar  
31 provisions of prior revenue laws provide that no loss may be recognized on an  
32 exchange of properties of a type described in section 1031, section 1035(a), section  
33 1036(a), or section 1037(a), although the taxpayer receives other property or money  
34 from the transaction. However, the basis of the property or properties (other than  
35 money) received by the taxpayer is the basis (adjusted to the date of the exchange) of  
36 the property transferred, decreased by the amount of money received. This basis must  
37 be allocated to the properties received, and for this purpose there must be allocated to





# EXETER

1031 Exchange Services LLC

1 such other property an amount of such basis equivalent to its fair market value at the  
2 date of the exchange.

3  
4 (e) If, upon an exchange of properties of the type described in section 1031, section  
5 1035(a), section 1036(a), or section 1037(a), the taxpayer also exchanged other  
6 property (not permitted to be transferred without the recognition of gain or loss) and  
7 gain or loss from the transaction is recognized under section 1002 or a similar  
8 provision of a prior revenue law, the basis of the property acquired is the total basis of  
9 the properties transferred (adjusted to the date of the exchange) increased by the  
10 amount of gain and decreased by the amount of loss recognized on the other property.  
11 For purposes of this rule, the taxpayer is deemed to have received in exchange for  
12 such other property an amount equal to its fair market value on the date of the  
13 exchange. The application of this paragraph may be illustrated by the following  
14 example:

15  
16 Example. A exchanges real estate held for investment plus stock for real estate to be  
17 held for investment. The real estate transferred has an adjusted basis of \$ 10,000 and  
18 a fair market value of \$ 11,000. The stock transferred has an adjusted basis of \$  
19 4,000 and a fair market value of \$ 2,000. The real estate acquired has a fair market  
20 value of \$ 13,000. A is deemed to have received a \$ 2,000 portion of the acquired real  
21 estate in exchange for the stock, since \$ 2,000 is the fair market value of the stock at  
22 the time of the exchange. A \$ 2,000 loss is recognized under section 1002 on the  
23 exchange of the stock for real estate. No gain or loss is recognized on the exchange of  
24 the real estate since the property received is of the type permitted to be received  
25 without recognition of gain or loss. The basis of the real estate acquired by A is  
26 determined as follows:  
27

Adjusted basis of real estate transferred	\$10,000
Adjusted basis of stock transferred	4,000
	-----
	14,000
Less: Loss recognized on transfer of stock	2,000
Basis of real estate acquired upon the exchange	12,000

28  
29 § 1.1031(d)-1T Coordination of section 1060 with section 1031 (temporary)

30  
31 If the properties exchanged under section 1031 are part of a group of assets which  
32 constitute a trade or business under section 1060, the like-kind property and other  
33 property or money which are treated as transferred in exchange for the like-kind  
34 property shall be excluded from the allocation rules of section 1060. However, section  
35 1060 shall apply to property which is not like-kind property or other property or  
36 money which is treated as transferred in exchange for the like-kind property. For  
37 application of the section 1060 allocation rules to property which is not part of the  
38 like-kind exchange, see § 1.1060-1(b), (c), and (d)





# EXETER

1031 Exchange Services LLC

1  
2 § 1.1031(d)-2 Treatment of assumption of liabilities  
3

4 For the purposes of section 1031(d), the amount of any liabilities of the taxpayer  
5 assumed by the other party to the exchange (or of any liabilities to which the property  
6 exchanged by the taxpayer is subject) is to be treated as money received by the  
7 taxpayer upon the exchange, whether or not the assumption resulted in a recognition  
8 of gain or loss to the taxpayer under the law applicable to the year in which the  
9 exchange was made. The application of this section may be illustrated by the following  
10 examples:

11  
12 Example 1. B, an individual, owns an apartment house which has an adjusted basis  
13 in his hands of \$ 500,000, but which is subject to a mortgage of \$ 150,000. On  
14 September 1, 1954, he transfers the apartment house to C, receiving in exchange  
15 therefor \$ 50,000 in cash and another apartment house with a fair market value on  
16 that date of \$ 600,000. The transfer to C is made subject to the \$ 150,000 mortgage. B  
17 realizes a gain of \$ 300,000 on the exchange, computed as follows:

Value of property received	\$ 600,000
Cash	50,000
Liabilities subject to which old property was transferred	150,000
Total consideration received	800,000
Less: Adjusted basis of property transferred	500,000
Gain realized	300,000
Under section 1031(b), \$200,000 of the \$300,000 gain is recognized. The basis of the apartment house acquired by B upon the exchange is \$500,000, computed as follows: Adjusted basis of property transferred	500,000
Less: Amount of money received:	
Cash	\$ 50,000
Amount of liabilities subject to which property was transferred	150,000
	200,000
Difference	----- 300,000
Plus: Amount of gain recognized upon the exchange	200,000
Basis of property acquired upon the exchange	500,000



# EXETER

1031 Exchange Services LLC

1  
2  
3 Example 2. (a) D, an individual, owns an apartment house. On December 1, 1955, the  
4 apartment house owned by D has an adjusted basis in his hands of \$ 100,000, a fair  
5 market value of \$ 220,000, but is subject to a mortgage of \$ 80,000. E, an individual,  
6 also owns an apartment house. On December 1, 1955, the apartment house owned by  
7 E has an adjusted basis of \$ 175,000, a fair market value of \$ 250,000, but is subject  
8 to a mortgage of \$ 150,000. On December 1, 1955, D transfers his apartment house to  
9 E, receiving in exchange therefore \$ 40,000 in cash and the apartment house owned  
10 by E. Each apartment house is transferred subject to the mortgage on it.  
11  
12 (b) D realizes a gain of \$ 120,000 on the exchange, computed as follows:

Value of property received	-----	\$ 250,000
Cash	40,000	
Liabilities subject to which old property was transferred	80,000	-----
Total consideration received	370,000	
Less:		
Adjusted basis of property transferred	\$ 100,000	
Liabilities to which new property is subject	150,000	
	250,000	
Gain realized	-----	120,000

13  
14 For purposes of section 1031(b), the amount of other property or money received by D  
15 is \$40,000. (Consideration received by D in the form of a transfer subject to a liability  
16 of \$ 80,000 is offset by consideration given in the form of a receipt of property subject  
17 to a \$ 150,000 liability. Thus, only the consideration received in the form of cash,  
18 \$40,000 is treated as other property or money for purposes of section 1031(b).)  
19 Accordingly, under section 1031(b), \$40,000 of the \$120,000 gain is recognized. The  
20 basis of the apartment house acquired by D is \$ 170,000, computed as follows:

Adjusted basis of property transferred	\$ 100,000	
Liabilities to which new property is subject	150,000	-----
Total	250,000	
Less: Amount of money received: Cash	\$ 40,000	
Amount of liabilities subject to which property was transferred	80,000	

		120,000	
Difference		130,000	
Plus: Amount of gain recognized upon the exchange		40,000	-----
Basis of property acquired upon the exchange		170,000	

1  
2 (c) E realizes a gain of \$ 75,000 on the exchange, computed as follows:

Value of property received		\$ 220,000	
Liabilities subject to which old property was transferred		150,000	-----
Total consideration received		370,000	
Less:			
Adjusted basis of property transferred		\$ 175,000	
Cash		40,000	
Liabilities to which new property is subject		80,000	
		295,000	
Gain realized		75,000	

3  
4 For purposes of section 1031(b), the amount of other property or money received by E  
5 is \$ 30,000. (Consideration received by E in the form of a transfer subject to a liability  
6 of \$ 150,000 is offset by consideration given in the form of a receipt of property subject  
7 to an \$ 80,000 liability and by the \$ 40,000 cash paid by E. Although consideration  
8 received in the form of cash or other property is not offset by consideration given in  
9 the form of an assumption of liabilities or a receipt of property subject to a liability,  
10 consideration given in the form of cash or other property is offset against  
11 consideration received in the form of an assumption of liabilities or a transfer of  
12 property subject to a liability.) Accordingly, under section 1031(b), \$ 30,000 of the \$  
13 75,000 gain is recognized. The basis of the apartment house acquired by E is \$  
14 175,000, computed as follows:

Adjusted basis of property transferred		\$ 175,000	
Cash		40,000	
Liabilities to which new property is subject		80,000	-----
Total		295,000	

Less: Amount of money received: Amount of liabilities subject to which property was



# EXETER

1031 Exchange Services LLC

Transferred	\$ 150,000	
	150,000	
Difference	145,000	
Plus: Amount of gain recognized upon the exchange	30,000	-----
Basis of property acquired upon the exchange	175,000	

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28  
29  
30  
31  
32  
33  
34  
35  
36  
37  
38  
39

## § 1.1031(e)-1 Exchanges of livestock of the different sexes.

Section 1031(e) provides that livestock of different sexes are not property of like kind. Section 1031(e) and this section are applicable to taxable years to which the Internal Revenue Code of 1954 applies.

## § 1.1031(j)-1 Exchanges of multiple properties.

### (a) Introduction –

#### (1) Overview.

As a general rule, the application of section 1031 requires a property-by-property comparison for computing the gain recognized and basis of property received in a like-kind exchange. This section provides an exception to this general rule in the case of an exchange of multiple properties. An exchange is an exchange of multiple properties if, under paragraph (b)(2) of this section, more than one exchange group is created. In addition, an exchange is an exchange of multiple properties if only one exchange group is created but there is more than one property being transferred or received within that exchange group. Paragraph (b) of this section provides rules for computing the amount of gain recognized in an exchange of multiple properties qualifying for nonrecognition of gain or loss under section 1031. Paragraph (c) of this section provides rules for computing the basis of properties received in an exchange of multiple properties qualifying for nonrecognition of gain or loss under section 1031.

#### (2) General approach.

(i) In general, the amount of gain recognized in an exchange of multiple properties is computed by first separating the properties transferred and the properties received by the taxpayer in the exchange into exchange groups in the manner described in paragraph (b)(2) of this section. The separation of the properties transferred and the properties received in the exchange into exchange groups involves matching up properties of a like kind of like class to the extent possible. Next, all liabilities assumed by the taxpayer as part of the transaction are offset by all liabilities of which the taxpayer is relieved as part of the transaction, with the excess liabilities assumed or relieved allocated in accordance with paragraph (b)(2)(ii) of this section. Then, the rules of section 1031 and the regulations thereunder are applied separately to each exchange group to determine the amount of gain recognized in the exchange. See §§



# EXETER

1031 Exchange Services LLC

1 1.1031(b)-1 and 1.1031(c)-1. Finally, the rules of section 1031 and the regulations  
2 thereunder are applied separately to each exchange group to determine the basis of  
3 the properties received in the exchange. See §§ 1.1031(d)-1 and 1.1031(d)-2.  
4

5 (ii) For purposes of this section, the exchanges are assumed to be made at arms'  
6 length, so that the aggregate fair market value of the property received in the exchange  
7 equals the aggregate fair market value of the property transferred. Thus, the amount  
8 realized with respect to the properties transferred in each exchange group is assumed  
9 to equal their aggregate fair market value.

10  
11 (b) Computation of gain recognized --  
12

13 (1) In general.  
14

15 In computing the amount of gain recognized in an exchange of multiple properties, the  
16 fair market value must be determined for each property transferred and for each  
17 property received by the taxpayer in the exchange. In addition, the adjusted basis  
18 must be determined for each property transferred by the taxpayer in the exchange.  
19

20 (2) Exchange groups and residual group.  
21

22 The properties transferred and the properties received by the taxpayer in the exchange  
23 are separated into exchange groups and a residual group to the extent provided in this  
24 paragraph (b)(2).  
25

26 (i) Exchange groups. Each exchange group consists of the properties transferred and  
27 received in the exchange, all of which are of a like kind or like class. If a property  
28 could be included in more than one exchange group, the taxpayer may include the  
29 property in any of those exchange groups. Property eligible for inclusion within an  
30 exchange group does not include money or property described in section 1031(a)(2)  
31 (i.e., stock in trade or other property held primarily for sale, stocks, bonds, notes,  
32 other securities or evidences of indebtedness or interest, interests in a partnership,  
33 certificates of trust or beneficial interests, or choses in action). For example, an  
34 exchange group may consist of all exchanged properties that are within the same  
35 General Asset Class or within the same Product Class (as defined in § 1.1031(a)-2(b)).  
36 Each exchange group must consist of at least one property transferred and at least  
37 one property received in the exchange.  
38

39 (ii) Treatment of liabilities. (A) All liabilities assumed by the taxpayer as part of the  
40 exchange are offset against all liabilities of which the taxpayer is relieved as part of the  
41 exchange, regardless of whether the liabilities are recourse or nonrecourse and  
42 regardless of whether the liabilities are secured by or otherwise relate to specific  
43 property transferred or received as part of the exchange. See §§ 1.1031 (b)-1(c) and  
44 1.1031(d)-2. For purposes of this section, liabilities assumed by the taxpayer as part of  
45 the exchange consist of liabilities of the other party to the exchange assumed by the  
46 taxpayer and liabilities subject to which the other party's property is transferred in the  
47 exchange. Similarly, liabilities of which the taxpayer is relieved as part of the exchange



# EXETER

1031 Exchange Services LLC

1 consist of liabilities of the taxpayer assumed by the other party to the exchange and  
2 liabilities subject to which the taxpayer's property is transferred.

3  
4 (B) If there are excess liabilities assumed by the taxpayer as part of the exchange (i.e.,  
5 the amount of liabilities assumed by the taxpayer exceeds the amount of liabilities of  
6 which the taxpayer is relieved), the excess is allocated among the exchange groups  
7 (but not to the residual group) in proportion to the aggregate fair market value of the  
8 properties received by the taxpayer in the exchange groups. The amount of excess  
9 liabilities assumed by the taxpayer that are allocated to each exchange group may not  
10 exceed the aggregate fair market value of the properties received in the exchange  
11 group.

12  
13 (C) If there are excess liabilities of which the taxpayer is relieved as part of the  
14 exchange (i.e., the amount of liabilities of which the taxpayer is relieved exceeds the  
15 amount of liabilities assumed by the taxpayer), the excess is treated as a Class I asset  
16 for purposes of making allocations to the residual group under paragraph (b)(2)(iii) of  
17 this section.

18  
19 (D) Paragraphs (b)(2)(ii) (A), (B), and (C) of this section are applied in the same manner  
20 even if section 1031 and this section apply to only a portion of a larger transaction  
21 (such as a transaction described in section 1060(c) and § 1.1060-1T(b)). In that event,  
22 the amount of excess liabilities assumed by the taxpayer or the amount of excess  
23 liabilities of which the taxpayer is relieved is determined based on all liabilities  
24 assumed by the taxpayer and all liabilities of which the taxpayer is relieve as part of  
25 the larger transaction.

26  
27 (iii) Residual group. If the aggregate fair market value of the properties transferred in  
28 all of the exchange groups differs from the aggregate fair market value of the  
29 properties received in all of the exchange groups (taking liabilities into account in the  
30 manner described in paragraph (b)(2)(ii) of this section), a residual group is created.  
31 The residual group consists of an amount of money or other property having an  
32 aggregate fair market value equal to that difference. The residual group consists of  
33 either money or other property transferred in the exchange or money or other property  
34 received in the exchange, but not both. For this purpose, other property includes  
35 property described in section 1031(a)(2) (i.e., stock in trade or other property held  
36 primarily for sale, stocks, bonds, notes, other securities or evidences of indebtedness  
37 or interest, interests in a partnership, certificates of trust or beneficial interests, or  
38 choses in action), property transferred that is not of a like kind or like class with any  
39 property received, and property received that is not of a like kind or like class with any  
40 property transferred. The money and properties that are allocated to the residual  
41 group are considered to come from the following assets in the following order: first  
42 from Class I assets, then from Class II assets, then from Class III assets, and then  
43 from Class IV assets. The terms Class I assets, Class II assets, Class III assets, and  
44 Class IV assets have the same meanings as in § 1.338-6(b), to which reference is made  
45 by § 1.1060-1(c)(2). Within each Class, taxpayers may choose which properties are  
46 allocated to the residual group.





# EXETER

1031 Exchange Services LLC

1 (iv) Exchange group surplus and deficiency. For each of the exchange groups  
2 described in this section, an "exchange group surplus" or "exchange group deficiency,"  
3 if any, must be determined. An exchange group surplus is the excess of the aggregate  
4 fair market value of the properties received (less the amount of any excess liabilities  
5 assumed by the taxpayer that are allocated to that exchange group), in an exchange  
6 group over the aggregate fair market value of the properties transferred in that  
7 exchange group. An exchange group deficiency is the excess of the aggregate fair  
8 market value of the properties transferred in an exchange group over the aggregate fair  
9 market value of the properties received (less the amount of any excess liabilities  
10 assumed by the taxpayer that are allocated to that exchange group) in that exchange  
11 group.

12

13 (3) Amount of gain recognized. –

14

15 (i) For purposes of this section, the amount of gain or loss realized with respect to each  
16 exchange group and the residual group is the difference between the aggregate fair  
17 market value of the properties transferred in that exchange group or residual group  
18 and the properties' aggregate adjusted basis. The gain realized with respect to each  
19 exchange group is recognized to the extent of the lesser of the gain realized and the  
20 amount of the exchange group deficiency, if any. Losses realized with respect to an  
21 exchange group are not recognized. See section 1031 (a) and (c). The total amount of  
22 gain recognized under section 1031 in the exchange is the sum of the amount of gain  
23 recognized with respect to each exchange group. With respect to the residual group,  
24 the gain or loss realized (as determined under this section) is recognized as provided in  
25 section 1001 or other applicable provision of the Code.

26

27 (ii) The amount of gain or loss realized and recognized with respect to properties  
28 transferred by the taxpayer that are not within any exchange group or the residual  
29 group is determined under section 1001 and other applicable provisions of the Code,  
30 with proper adjustments made for all liabilities not allocated to the exchange groups or  
31 the residual group.

32

33 (c) Computation of basis of properties received.

34

35 In an exchange of multiple properties qualifying for nonrecognition of gain or loss  
36 under section 1031 and this section, the aggregate basis of properties received in each  
37 of the exchange groups is the aggregate adjusted basis of the properties transferred by  
38 the taxpayer within that exchange group, increased by the amount of gain recognized  
39 by the taxpayer with respect to that exchange group, increased by the amount of the  
40 exchange group surplus or decreased by the amount of the exchange group deficiency,  
41 and increased by the amount, if any, of excess liabilities assumed by the taxpayer that  
42 are allocated to that exchange group. The resulting aggregate basis of each exchange  
43 group is allocated proportionately to each property received in the exchange group in  
44 accordance with its fair market value. The basis of each property received within the  
45 residual group (other than money) is equal to its fair market value.

46

47 (d) Examples.





# EXETER

1031 Exchange Services LLC

1  
2 The application of this section may be illustrated by the following examples:  
3

4 Example 1. (i) K exchanges computer A (asset class 00.12) and automobile A (asset  
5 class 00.22), both of which were held by K for productive use in its business, with W  
6 for printer B (asset class 00.12) and automobile B (asset class 00.22), both of which  
7 will be held by K for productive use in its business. K's adjusted basis and the fair  
8 market value of the exchanged properties are as follows:

	<b>Adjusted basis</b>	<b>Fair market value</b>
Computer A	\$375	\$1,000
Automobile A	1,500	4,000
Printer B		2,050
Automobile B		2,950

9  
10 (ii) Under paragraph (b)(2) of this section, the properties exchanged are separated into  
11 exchange groups as follows:  
12

13 (A) The first exchange group consists of computer A and printer B (both are within the  
14 same General Asset Class) and, as to K, has an exchange group surplus of \$ 1050  
15 because the fair market value of printer B (\$ 2050) exceeds the fair market value of  
16 computer A (\$ 1000) by that amount.  
17

18 (B) The second exchange group consists of automobile A and automobile B (both are  
19 within the same General Asset Class) and, as to K, has an exchange group deficiency  
20 of \$ 1050 because the fair market value of automobile A (\$ 4000) exceeds the fair  
21 market value of automobile B (\$ 2950) by that amount.  
22

23 (iii) K recognizes gain on the exchange as follows:  
24

25 (A) With respect to the first exchange group, the amount of gain realized is the excess  
26 of the fair market value of computer A (\$ 1000) over its adjusted basis (\$ 375), or \$  
27 625. The amount of gain recognized is the lesser of the gain realized (\$ 625) and the  
28 exchange group deficiency (\$ 0), or \$ 0.  
29

30 (B) With respect to the second exchange group, the amount of gain realized is the  
31 excess of the fair market value of automobile A (\$ 4000) over its adjusted basis (\$  
32 1500), or \$ 2500. The amount of gain recognized is the lesser of the gain realized (\$  
33 2500) and the exchange group deficiency (\$ 1050), or \$ 1050.  
34

35 (iv) The total amount of gain recognized by K in the exchange is the sum of the gains  
36 recognized with respect to both exchange groups (\$ 0 + \$ 1050), or \$ 1050.  
37

38 (v) The bases of the property received by K in the exchange, printer B and automobile



# EXETER

1031 Exchange Services LLC

1 B, are determined in the following manner:  
2

3 (A) The basis of the property received in the first exchange group is the adjusted basis  
4 of the property transferred within the exchange group (\$ 375), increased by the  
5 amount of gain recognized with respect to that exchange group (\$ 0), increased by the  
6 amount of the exchange group surplus (\$ 1050), and increased by the amount of  
7 excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 1425. Because  
8 printer B was the only property received within the first exchange group, the entire  
9 basis of \$ 1425 is allocated to printer B.

10  
11 (B) The basis of the property received in the second exchange group is the adjusted  
12 basis of the property transferred within that exchange group (\$ 1500), increased by  
13 the amount of gain recognized with respect to that exchange group (\$ 1050), decreased  
14 by the amount of the exchange group deficiency (\$ 1050), and increased by the  
15 amount of excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 1500.  
16 Because automobile B was the only property received within the second exchange  
17 group, the entire basis of \$ 1500 is allocated to automobile B.  
18

19 Example 2. (i) F exchanges computer A (asset class 00.12) and automobile A (asset  
20 class 00.22), both of which were held by F for productive use in its business, with G  
21 for printer B (asset class 00.12) and automobile B (asset class 00.22), both of which  
22 will be held by F for productive use in its business, and corporate stock and \$ 500  
23 cash. The adjusted basis and fair market value of the properties are as follows:

	<b>Adjusted basis</b>	<b>Fair market value</b>
Computer A	\$375	\$1,000
Automobile A	3,500	4,000
Printer B		800
Automobile B		2,950
Corporate stock		750
Cash		500

24  
25 (ii) Under paragraph (b)(2) of this section, the properties exchanged are separated into  
26 exchange groups as follows:  
27

28 (A) The first exchange group consists of computer A and printer B (both are within the  
29 same General Asset Class) and, as to F, has an exchange group deficiency of \$ 200  
30 because the fair market value of computer A (\$ 1000) exceeds the fair market value of  
31 printer B (\$ 800) by that amount.  
32

33 (B) The second exchange group consists of automobile A and automobile B (both are  
34 within the same General Asset Class) and, as to F, has an exchange group deficiency  
35 of \$ 1050 because the fair market value of automobile A (\$ 4000) exceeds the fair  
36 market value of automobile B (\$ 2950) by that amount.



# EXETER

1031 Exchange Services LLC

1  
2 (C) Because the aggregate fair market value of the properties transferred by F in the  
3 exchange groups (\$ 5,000) exceeds the aggregate fair market value of the properties  
4 received by F in the exchange groups (\$ 3750) by \$ 1250, there is a residual group in  
5 that amount consisting of the \$ 500 cash and the \$ 750 worth of corporate stock.

6  
7 (iii) F recognizes gain on the exchange as follows:

8  
9 (A) With respect to the first exchange group, the amount of gain realized is the excess  
10 of the fair market value of computer A (\$ 1000) over its adjusted basis (\$ 375), or \$  
11 625. The amount of gain recognized is the lesser of the gain realized (\$ 625) and the  
12 exchange group deficiency (\$ 200), or \$ 200.

13  
14 (B) With respect to the second exchange group, the amount of gain realized is the  
15 excess of the fair market value of automobile A (\$ 4000) over its adjusted basis (\$  
16 3500), or \$ 500. The amount of gain recognized is the lesser of the gain realized (\$  
17 500) and the exchange group deficiency (\$ 1050), or \$ 500.

18  
19 (C) No property transferred by F was allocated to the residual group. Therefore, F does  
20 not recognize gain or loss with respect to the residual group.

21  
22 (iv) The total amount of gain recognized by F in the exchange is the sum of the gains  
23 recognized with respect to both exchange groups (\$ 200 + \$ 500), or \$ 700.

24  
25 (v) The bases of the properties received by F in the exchange (printer B, automobile B,  
26 and the corporate stock) are determined in the following manner:

27  
28 (A) The basis of the property received in the first exchange group is the adjusted basis  
29 of the property transferred within that exchange group (\$ 375), increased by the  
30 amount of gain recognized with respect to that exchange group (\$ 200), decreased by  
31 the amount of the exchange group deficiency (\$ 200), and increased by the amount of  
32 excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 375. Because  
33 printer B was the only property received within the first exchange group, the entire  
34 basis of \$ 375 is allocated to printer B.

35  
36 (B) The basis of the property received in the second exchange group is the adjusted  
37 basis of the property transferred within that exchange group (\$ 3500), increased by  
38 the amount of gain recognized with respect to that exchange group (\$ 500), decreased  
39 by the amount of the exchange group deficiency (\$ 1050), and increased by the  
40 amount of excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 2950.  
41 Because automobile B was the only property received within the second exchange  
42 group, the entire basis of \$ 2950 is allocated to automobile B.

43  
44 (C) The basis of the property received within the residual group (the corporate stock) is  
45 equal to its fair market value or \$ 750. Cash of \$ 500 is also received within the  
46 residual group.

47



# EXETER

1031 Exchange Services LLC

1 Example 3. (i) J and H enter into an exchange of the following properties. All of the  
2 property (except for the inventory) transferred by J was held for productive use in J's  
3 business. All of the property received by J will be held by J for productive use in its  
4 business.

**J Transfers:**

**H transfers:**

<b>Property</b>	<b>Adjusted basis</b>	<b>Fair market value</b>	<b>Property</b>	<b>Fair market value</b>
Computer A	\$1,500	\$5,000	Computer Z	\$4,500
Computer B	500	3,000	Printer Y	2,500
Printer C	2,000	1,500	Real Estate X	1,000
Real Estate D	1,200	2,000	Real Estate W	4,000
Real Estate E	0	1,800	Grader V	2,000
Scraper F	3,300	2,500	Truck T	1,700
Inventory	1,000	1,700	Cash	1,800
	-----	-----		-----
Total	9,500	17,500		17,500

5  
6  
7 (ii) Under paragraph (b)(2) of this section, the properties exchanged are separated into  
8 exchange groups as follows:  
9

10 (A) The first exchange group consists of computer A, computer B, printer C, computer  
11 Z, and printer Y (all are within the same General Asset Class) and, as to J, has an  
12 exchange group deficiency of \$ 2500 ((\$ 5000 + \$ 3000 + \$ 1500) - (\$ 4500 + \$ 2500)).  
13

14 (B) The second exchange group consists of real estate D, E, X and W (all are of a like  
15 kind) and, as to J, has an exchange group surplus of \$ 1200 ((\$ 1000 + \$ 4000) - (\$  
16 2000 + \$ 1800)).  
17

18 (C) The third exchange group consists of scraper F and grader V (both are within the  
19 same Product Class (NAICS code 333120)) and, as to J, has an exchange group  
20 deficiency of \$ 500 (\$ 2500 - \$ 2000).  
21

22 (D) Because the aggregate fair market value of the properties transferred by J in the  
23 exchange groups (\$ 15,800) exceeds the aggregate fair market value of the properties  
24 received by J in the exchange groups (\$ 14,000) by \$ 1800, there is a residual group in  
25 that amount consisting of the \$ 1800 cash (a Class I asset).  
26

27 (E) The transaction also includes a taxable exchange of inventory (which is property  
28 described in section 1031 (a)(2)) for truck T (which is not of a like kind or like class to  
29 any property transferred in the exchange).  
30



# EXETER

1031 Exchange Services LLC

1 (iii) J recognizes gain on the transaction as follows:  
2

3 (A) With respect to the first exchange group, the amount of gain realized is the excess  
4 of the aggregate fair market value of the properties transferred in the exchange group  
5 (\$ 9500) over the aggregate adjusted basis (\$ 4000), or \$ 5500. The amount of gain  
6 recognized is the lesser of the gain realized (\$ 5500) and the exchange group deficiency  
7 (\$ 2500), or \$ 2500.  
8

9 (B) With respect to the second exchange group, the amount of gain realized is the  
10 excess of the aggregate fair market value of the properties transferred in the exchange  
11 group (\$ 3800) over the aggregate adjusted basis (\$ 1200), or \$ 2600. The amount of  
12 gain recognized is the lesser of the gain realized (\$ 2600) and the exchange group  
13 deficiency (\$ 0), or \$ 0.  
14

15 (C) With respect to the third exchange group, a loss is realized in the amount of \$ 800  
16 because the fair market value of the property transferred in the exchange group (\$  
17 2500) is less than its adjusted basis (\$ 3300). Although a loss of \$ 800 was realized,  
18 under section 1031 (a) and (c) losses are not recognized.  
19

20 (D) No property transferred by J was allocated to the residual group. Therefore, J does  
21 not recognize gain or loss with respect to the residual group.  
22

23 (E) With respect to the taxable exchange of inventory for truck T, gain of \$ 700 is  
24 realized and recognized by J (amount realized of \$ 1700 (the fair market value of truck  
25 T) less the adjusted basis of the inventory (\$ 1000)).  
26

27 (iv) The total amount of gain recognized by J in the transaction is the sum of the gains  
28 recognized under section 1031 with respect to each exchange group (\$ 2500 + \$ 0 + \$  
29 0) and any gain recognized outside of section 1031 (\$ 700), or \$ 3200.  
30

31 (v) The bases of the property received by J in the exchange are determined in the  
32 following manner:  
33

34 (A) The aggregate basis of the properties received in the first exchange group is the  
35 adjusted basis of the properties transferred within that exchange group (\$ 4000),  
36 increased by the amount of gain recognized with respect to that exchange group (\$  
37 2500), decreased by the amount of the exchange group deficiency (\$ 2500), and  
38 increased by the amount of excess liabilities assumed allocated to that exchange  
39 group (\$ 0), or \$ 4000. This \$ 4000 of basis is allocated proportionately among the  
40 assets received within the first exchange group in accordance with their fair market  
41 values: Computer Z's basis is \$ 2571 ( $\$ 4000 \times \$ 4500 / \$ 7000$ ); printer Y's basis is \$  
42 1429 ( $\$ 4000 \times \$ 2500 / \$ 7000$ ).  
43

44 (B) The aggregate basis of the properties received in the second exchange group is the  
45 adjusted basis of the properties transferred within that exchange group (\$ 1200),  
46 increased by the amount of gain recognized with respect to that exchange group (\$ 0),  
47 increased by the amount of the exchange group surplus (\$ 1200), and increased by



# EXETER

1031 Exchange Services LLC

1 the amount of excess liabilities assumed allocated to that exchange group (\$ 0), or \$  
2 2400. This \$ 2400 of basis is allocated proportionately among the assets received  
3 within the second exchange group in accordance with their fair market values: Real  
4 estate X's basis is \$ 480 ( $\$ 2400 \times \$ 1000 / \$ 5000$ ); real estate W's basis is \$ 1920 ( $\$$   
5  $2400 \times \$ 4000 / \$ 5000$ ).  
6

7 (c) The basis of the property received in the third exchange group is the adjusted basis  
8 of the property transferred within that exchange group (\$ 3300), increased by the  
9 amount of gain recognized with respect to that exchange group (\$ 0), decreased by the  
10 amount of the exchange group deficiency (\$ 500), and increased by the amount of  
11 excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 2800. Because  
12 grader V was the only property received within the third exchange group, the entire  
13 basis of \$ 2800 is allocated to grader V.  
14

15 (D) Cash of \$ 1800 is received within the residual group.  
16

17 (E) The basis of the property received in the taxable exchange (truck T) is equal to its  
18 cost of \$ 1700.  
19

20 Example 4. (i) B exchanges computer A (asset class 00.12), automobile A (asset class  
21 00.22) and truck A (asset class 00.241), with C for computer R (asset class 00.12),  
22 automobile R (asset class 00.22), truck R (asset class 00.241) and \$ 400 cash. All  
23 properties transferred by either B or C were held for productive use in the respective  
24 transferor's business. Similarly, all properties to be received by either B or C will be  
25 held for productive use in the respective recipient's business. Automobile A,  
26 automobile R and truck R are each secured by a nonrecourse liability and are  
27 transferred subject to such liability. The adjusted basis, fair market value, and liability  
28 secured by each property, if any, are as follows:

	<b>Adjusted basis</b>	<b>Fair market value</b>	<b>Liability</b>
B transfers:			
Computer A	\$800	\$1,500	\$0
Automobile A	900	2,500	500
Truck A	700	2,000	0
C transfers:			
Computer R	1,100	1,600	0
Automobile R	2,100	3,100	750
Truck R	600	1,400	250
Cash		400	

29  
30  
31 (ii) The tax treatment to B is as follows:





# EXETER

1031 Exchange Services LLC

- 1  
2 (A)(1) The first exchange group consists of computers A and R (both are within the  
3 same General Asset Class).  
4  
5 (2) The second exchange group consists of automobiles A and R (both are within the  
6 same General Asset Class).  
7  
8 (3) The third exchange group consists of trucks A and R (both are in the same General  
9 Asset Class).

10  
11 (B) Under paragraph (b)(2)(ii) of this section, all liabilities assumed by B (\$ 1000) are  
12 offset by all liabilities of which B is relieved (\$ 500), resulting in excess liabilities  
13 assumed of \$ 500. The excess liabilities assumed of \$ 500 is allocated among the  
14 exchange groups in proportion to the fair market value of the properties received by B  
15 in the exchange groups as follows:

16  
17 (1) \$ 131 of excess liabilities assumed ( $\$ 500 \times \$ 1600 / \$ 6100$ ) is allocated to the first  
18 exchange group. The first exchange group has an exchange group deficiency of \$ 31  
19 because the fair market value of computer A (\$ 1500) exceeds the fair market value of  
20 computer R less the excess liabilities assumed allocated to the exchange group ( $\$$   
21  $1600 - \$ 131$ ) by that amount.

22  
23 (2) \$ 254 of excess liabilities assumed ( $\$ 500 \times \$ 3100 / \$ 6100$ ) is allocated to the  
24 second exchange group. The second exchange group has an exchange group surplus  
25 of \$ 346 because the fair market value of automobile R less the excess liabilities  
26 assumed allocated to the exchange group ( $\$ 3100 - \$ 254$ ) exceeds the fair market value  
27 of automobile A (\$ 2500) by that amount.

28  
29 (3) \$ 115 of excess liabilities assumed ( $\$ 500 \times \$ 1400 / \$ 6100$ ) is allocated to the third  
30 exchange group. The third exchange group has an exchange group deficiency of \$ 715  
31 because the fair market value of truck A (\$ 2000) exceeds the fair market value of  
32 truck R less the excess liabilities assumed allocated to the exchange group ( $\$ 1400 - \$$   
33  $115$ ) by that amount.

34  
35 (4) The difference between the aggregate fair market value of the properties transferred  
36 in all of the exchange groups, \$ 6000, and the aggregate fair market value of the  
37 properties received in all of the exchange groups (taking excess liabilities assumed into  
38 account), \$ 5600, is \$ 400. Therefore there is a residual group in that amount  
39 consisting of \$ 400 cash received.

40  
41 (C) B recognizes gain on the exchange as follows:

42  
43 (1) With respect to the first exchange group, the amount of gain realized is the excess  
44 of the fair market value of computer A (\$ 1500) over its adjusted basis (\$ 800), or \$  
45 700. The amount of gain recognized is the lesser of the gain realized (\$ 700) and the  
46 exchange group deficiency (\$ 31), or \$ 31.

47





# EXETER

1031 Exchange Services LLC

1 (2) With respect to the second exchange group, the amount of gain realized is the  
2 excess of the fair market value of automobile A (\$ 2500) over its adjusted basis (\$ 900),  
3 or \$ 1600.

4  
5 The amount of gain recognized is the lesser of the gain realized (\$ 1600) and the  
6 exchange group deficiency (\$ 0), or \$ 0.

7  
8 (3) With respect to the third exchange group, the amount of gain realized is the excess  
9 of the fair market value of truck A (\$ 2000) over its adjusted basis (\$ 700), or \$ 1300.  
10 The amount of gain recognized is the lesser of gain realized (\$ 1300) and the exchange  
11 group deficiency (\$ 715), or \$ 715.

12  
13 (4) No property transferred by B was allocated to the residual group. Therefore, B does  
14 not recognize gain or loss with respect to the residual group.

15  
16 (D) The total amount of gain recognized by B in the exchange is the sum of the gains  
17 recognized under section 1031 with respect to each exchange group (\$ 31 + \$ 0 + \$  
18 715), or \$ 746.

19  
20 (E) the bases of the property received by B in the exchange (computer R, automobile R,  
21 and truck R) are determined in the following manner:

22  
23 (1) The basis of the property received in the first exchange group is the adjusted basis  
24 of the property transferred within that exchange group (\$ 800), increased by the  
25 amount of gain recognized with respect to that exchange group (\$ 31), decreased by  
26 the amount of the exchange group deficiency (\$ 31), and increased by the amount of  
27 excess liabilities assumed allocated to that exchange group (\$ 131), or \$ 931. Because  
28 computer R was the only property received within the first exchange group, the entire  
29 basis of \$ 931 is allocated to computer R.

30  
31 (2) The basis of the property received in the second exchange group is the adjusted  
32 basis of the property transferred within that exchange group (\$ 900), increased by the  
33 amount of gain recognized with respect to that exchange group (\$ 0), increased by the  
34 amount of the exchange group surplus (\$ 346), and increased by the amount of excess  
35 liabilities assumed allocated to that exchange group (\$ 254), or \$ 1500. Because  
36 automobile R was the only property received within the second exchange group, the  
37 entire basis of \$ 1500 is allocated to automobile R.

38  
39 (3) The basis of the property received in the third exchange group is the adjusted basis  
40 of the property transferred within that exchange group (\$ 700), increased by the  
41 amount of gain recognized with respect to that exchange group (\$ 715), decreased by  
42 the amount of the exchange group deficiency (\$ 715), and increased by the amount of  
43 excess liabilities assumed allocated to that exchange group (\$ 115), or \$ 815. Because  
44 truck R was the only property received within the third exchange group, the entire  
45 basis of \$ 815 is allocated to truck R.

46  
47 (F) Cash of \$ 400 is also received by B.



# EXETER

1031 Exchange Services LLC

- 1  
2 (iii) The tax treatment to C is as follows:  
3  
4 (A) (1) The first exchange group consists of computers R and A (both are within the  
5 same General Asset Class).  
6  
7 (2) The second exchange group consists of automobiles R and A (both are within the  
8 same General Asset Class).  
9  
10 (3) The third exchange group consists of trucks R and A (both are in the same General  
11 Asset Class).

12  
13 (B) Under paragraph (b)(2)(ii) of this section, all liabilities of which C is relieved (\$  
14 1000) are offset by all liabilities assumed by C (\$ 500), resulting in excess liabilities  
15 relieved of \$ 500. This excess liabilities relieved is treated as cash received by C.

16  
17 (1) The first exchange group has an exchange group deficiency of \$ 100 because the  
18 fair market value of computer R (\$ 1600) exceeds the fair market value of computer A  
19 (\$ 1500) by that amount.

20  
21 (2) The second exchange group has an exchange group deficiency of \$ 600 because the  
22 fair market value of automobile R (\$ 3100) exceeds the fair market value of automobile  
23 A (\$ 2500) by that amount.

24  
25 (3) The third exchange group has an exchange group surplus of \$ 600 because the fair  
26 market value of truck A (\$ 2000) exceeds the fair market value of truck R (\$ 1400) by  
27 that amount.

28  
29 (4) The difference between the aggregate fair market value of the properties transferred  
30 by C in all of the exchange groups, \$ 6100, and the aggregate fair market value of the  
31 properties received by C in all of the exchange groups, \$ 6000, is \$ 100. Therefore,  
32 there is a residual group in that amount, consisting of excess liabilities relieved of \$  
33 100, which is treated as cash received by C.

34  
35 (5) The \$ 400 cash paid by C and \$ 400 of the excess liabilities relieved which is  
36 treated as cash received by C are not within the exchange groups of the residual  
37 group.

38  
39 (C) C recognizes gain on the exchange as follows:

40  
41 (1) With respect to the first exchange group, the amount of gain realized is the excess  
42 of the fair market value of computer R (\$ 1600) over its adjusted basis (\$ 1100), or \$  
43 500. The amount of gain recognized is the lesser of the gain realized (\$ 500) and the  
44 exchange group deficiency (\$ 100), or \$ 100.

45  
46 (2) With respect to the second exchange group, the amount of gain realized is the  
47 excess of the fair market value of automobile R (\$ 3100) over its adjusted basis (\$



# EXETER

1031 Exchange Services LLC

1 2100), or \$ 1000. The amount of gain recognized is the lesser of the gain realized (\$  
2 1000) and the exchange group deficiency (\$ 600), or \$ 600.

3  
4 (3) With respect to the third exchange group, the amount of gain realized is the excess  
5 of the fair market value of truck R (\$ 1400) over its adjusted basis (\$ 600), or \$ 800.  
6 The amount of gain recognized is the lesser of gain realized (\$ 800) and the exchange  
7 group deficiency (\$ 0), or \$ 0.

8  
9 (4) No property transferred by C was allocated to the residual group. Therefore, C does  
10 not recognize any gain with respect to the residual group.

11  
12 (D) The total amount of gain recognized by C in the exchange is the sum of the gains  
13 recognized under section 1031 with respect to each exchange group (\$ 100+\$ 600+\$  
14 0), or \$ 700.

15  
16 (E) The bases of the properties received by C in the exchange (computer A, automobile  
17 A, and truck A) are determined in the following manner:

18  
19 (1) The basis of the property received in the first exchange group is the adjusted basis  
20 of the property transferred within that exchange group (\$ 1100), increased by the  
21 amount of gain recognized with respect to that exchange group (\$ 100), decreased by  
22 the amount of the exchange group deficiency (\$ 100), and increased by the amount of  
23 excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 1100. Because  
24 computer A was the only property received within the first exchange group, the entire  
25 basis of \$ 1100 is allocated to computer A.

26  
27 (2) The basis of the property received in the second exchange group is the adjusted  
28 basis of the property transferred within that exchange group (\$ 2100), increased by  
29 the amount of gain recognized with respect to that exchange group (\$ 600), decreased  
30 by the amount of the exchange group deficiency (\$ 600), and increased by the amount  
31 of excess liabilities assumed allocated to that exchange group (\$ 0), or \$ 2100.  
32 Because automobile A was the only property received within the second exchange  
33 group, the entire basis of \$ 2100 is allocated to automobile A.

34  
35 (3) The basis of the property received in the third exchange group is the adjusted basis  
36 of the property transferred within that exchange group (\$ 600), increased by the  
37 amount of gain recognized with respect to that exchange group (\$ 0), increased by the  
38 amount of the exchange group surplus (\$ 600), and increased by the amount of excess  
39 liabilities assumed allocated to that exchange group (\$ 0), or \$ 1200. Because truck A  
40 was the only property received within the third exchange group, the entire basis of \$  
41 1200 is allocated to truck A.

42  
43 Example 5. (i) U exchanges real estate A, real estate B, and grader A (NAICS code  
44 333120) with V for real estate R and railroad car R (General Asset Class 00.25). All  
45 properties transferred by either U or V were held for productive use in the respective  
46 transferor's business. Similarly, all properties to be received by either U or V will be  
47 held for productive use in the respective recipient's business. Real estate R is secured



# EXETER

1031 Exchange Services LLC

1 by a recourse liability and is transferred subject to that liability. The adjusted basis,  
2 fair market value, and liability secured by each property, if any, are as follows:

	<b>Adjusted basis</b>	<b>Fair market value</b>	<b>Liability</b>
U Transfers:			
Real Estate A	\$2000	\$5000	
Real Estate B	8000	13,500	
Grader A	500	2000	
V Transfers:			
Real Estate R	\$20,000	\$26,500	\$7000
Railroad car R	1200	1000	

3  
4 (ii) The tax treatment to U is as follows:

5  
6 (A) The exchange group consists of real estate A, real estate B, and real estate R.

7  
8 (B) Under paragraph (b)(2)(ii) of this section, all liabilities assumed by U (\$ 7000) are  
9 excess liabilities assumed. The excess liabilities assumed of \$ 7000 is allocated to the  
10 exchange group.

11  
12 (1) The exchange group has an exchange group surplus of \$ 1000 because the fair  
13 market value of real estate R less the excess liabilities assumed allocated to the  
14 exchange group (\$ 26,500-\$ 7000) exceeds the aggregate fair market value of real  
15 estate A and B (\$ 18,500) by that amount.

16  
17 (2) The difference between the aggregate fair market value of the properties received in  
18 the exchange group (taking excess liabilities assumed into account), \$ 19,500, and the  
19 aggregate fair market value of the properties transferred in the exchange group, \$  
20 18,500, is \$ 1000. Therefore, there is a residual group in that amount consisting of \$  
21 1000 (or 50 percent of the fair market value) of grader A.

22  
23 (3) The transaction also includes a taxable exchange of the 50 percent portion of  
24 grader A not allocated to the residual group (which is not of a like kind or like class to  
25 any property received by U in the exchange) for railroad car R (which is not of a like  
26 kind or like class to any property transferred by U in the exchange).

27  
28 (C) U recognizes gain on the exchange as follows:

29  
30 (1) With respect to the exchange group, the amount of the gain realized is the excess of  
31 the aggregate fair market value of real estate A and B (\$ 18,500) over the aggregate  
32 adjusted basis (\$ 10,000), or \$ 8500. The amount of the gain recognized is the lesser  
33 of the gain realized (\$ 8500) and the exchange group deficiency (\$ 0), or \$ 0.

34



# EXETER

1031 Exchange Services LLC

1 (2) With respect to the residual group, the amount of gain realized and recognized is  
2 the excess of the fair market value of the 50 percent portion of grader A that is  
3 allocated to the residual group (\$ 1000) over its adjusted basis (\$ 250), or \$ 750.

4  
5 (3) With respect to the taxable exchange of the 50 percent portion of grader A not  
6 allocated to the residual group for railroad car R, gain of \$ 750 is realized and  
7 recognized by U (amount realized of \$ 1000 (the fair market value of railroad car R)  
8 less the adjusted basis of the 50 percent portion of grader A not allocated to the  
9 residual group (\$ 250)).

10  
11 (D) The total amount of gain recognized by U in the transaction is the sum of the gain  
12 recognized under section 1031 with respect to the exchange group (\$ 0), any gain  
13 recognized with respect to the residual group (\$ 750), and any gain recognized with  
14 respect to property transferred that is not in the exchange group or the residual group  
15 (\$ 750), or \$ 1500.

16  
17 (E) The bases of the property received by U in the exchange (real estate R and railroad  
18 car R) are determined in the following manner:

19  
20 (1) The basis of the property received in the exchange group is the aggregate adjusted  
21 basis of the property transferred within that exchange group (\$ 10,000), increased by  
22 the amount of gain recognized with respect to that exchange group (\$ 0), increased by  
23 the amount of the exchange group surplus (\$ 1000), and increased by the amount of  
24 excess liabilities assumed allocated to that exchange group (\$ 7000), or \$ 18,000.  
25 Because real estate R is the only property received within the exchange group, the  
26 entire basis of \$ 18,000 is allocated to real estate R.

27  
28 (2) The basis of railroad car R is equal to its cost of \$ 1000.

29  
30 (iii) The tax treatment to V is as follows:

31  
32 (A) The exchange group consists of real estate R, real estate A, and real estate B.

33  
34 (B) Under paragraph (b)(2)(ii) of this section, the liabilities of which V is relieved (\$  
35 7000) results in excess liabilities relieved of \$ 7000 and is treated as cash received by  
36 V.

37  
38 (1) The exchange group has an exchange group deficiency of \$ 8000 because the fair  
39 market value of real estate R (\$ 26,500) exceeds the aggregate fair market value of real  
40 estate A and B (\$ 18,500) by that amount.

41  
42 (2) The difference between the aggregate fair market value of the properties transferred  
43 by V in the exchange group, \$ 26,500, and the aggregate fair market value of the  
44 properties received by V in the exchange group, \$ 18,500, is \$ 8000. Therefore, there  
45 is a residual group in that amount, consisting of the excess liabilities relieved of \$  
46 7000, which is treated as cash received by V, and \$ 1000 (or 50 percent of the fair  
47 market value) of grader A.



# EXETER

1031 Exchange Services LLC

1  
2 (3) The transaction also includes a taxable exchange of railroad car R (which is not of a  
3 like kind or like class to any property received by V in the exchange) for the 50 percent  
4 portion of grader A (which is not of a like kind or like class to any property transferred  
5 by V in the exchange) not allocated to the residual group.

6  
7 (C) V recognizes gain on the exchange as follows:

8  
9 (1) With respect to the exchange group, the amount of the gain realized is the excess of  
10 the fair market value of real estate R (\$ 26,500) over its adjusted basis (\$ 20,000), or \$  
11 6500. The amount of the gain recognized is the lesser of the gain realized (\$ 6500) and  
12 the exchange group deficiency (\$ 8000), or \$ 6500.

13  
14 (2) No property transferred by V was allocated to the residual group. Therefore, V does  
15 not recognize gain or loss with respect to the residual group.

16  
17 (3) With respect to the taxable exchange of railroad car R for the 50 percent portion of  
18 grader A not allocated to the exchange group or the residual group, a loss is realized  
19 and recognized in the amount of \$ 200 (the excess of the \$ 1200 adjusted basis of  
20 railroad car R over the amount realized of \$ 1000 (fair market value of the 50 percent  
21 portion of grader A)).

22  
23 (D) The basis of the property received by V in the exchange (real estate A, real estate B,  
24 and grader A) are determined in the following manner:

25  
26 (1) The basis of the property received in the exchange group is the adjusted basis of  
27 the property transferred within that exchange group (\$ 20,000), increased by the  
28 amount of gain recognized with respect to that exchange group (\$ 6500), and  
29 decreased by the amount of the exchange group deficiency (\$ 8000), or \$ 18,500. This  
30 \$ 18,500 of basis is allocated proportionately among the assets received within the  
31 exchange group in accordance with their fair market values: real estate A's basis is \$  
32 5000 ( $\$ 18,500 \times \$ 5000 / \$ 18,500$ ); real estate B's basis is \$ 13,500 ( $\$ 18,500 \times$   
33  $13,500 / \$ 18,500$ ).

34  
35 (2) The basis of grader A is \$ 2000.

36  
37 (e) Effective date.

38  
39 Section 1.1031 (j)-1 is effective for exchanges occurring on or after April 11, 1991.

40  
41 § 1.1031(K)-1 Treatment of deferred exchanges.

42  
43 (a) Overview.

44  
45 This section provides rules for the application of section 1031 and the regulations  
46 thereunder in the case of a "deferred exchange." For purposes of section 1031 and this  
47 section, a deferred exchange is defined as an exchange in which, pursuant to an





# EXETER

1031 Exchange Services LLC

1 agreement, the taxpayer transfers property held for productive use in a trade or  
2 business or for investment (the "relinquished property") and subsequently receives  
3 property to be held either for productive use in a trade or business or for investment  
4 (the "replacement property"). In the case of a deferred exchange, if the requirements  
5 set forth in paragraphs (b), (c), and (d) of this section (relating to identification and  
6 receipt of replacement property) are not satisfied, the replacement property received by  
7 the taxpayer will be treated as property which is not of a like kind to the relinquished  
8 property. In order to constitute a deferred exchange, the transaction must be an  
9 exchange (i.e., a transfer of property for property, as distinguished from a transfer of  
10 property for money). For example, a sale of property followed by a purchase of property  
11 of a like kind does not qualify for nonrecognition of gain or loss under section 1031  
12 regardless of whether the identification and receipt requirements of section 1031(a)(3)  
13 and paragraphs (b), (c), and (d) of this section are satisfied. The transfer of  
14 relinquished property in a deferred exchange is not within the provisions of section  
15 1031(a) if, as part of the consideration, the taxpayer receives money or property which  
16 does not meet the requirements of section 1031(a), but the transfer, if otherwise  
17 qualified, will be within the provisions of either section 1031 (b) or (c). See § 1.1031(a)-  
18 1(a)(2). In addition, in the case of a transfer of relinquished property in a deferred  
19 exchange, gain or loss may be recognized if the taxpayer actually or constructively  
20 receives money or property which does not meet the requirements of section 1031(a)  
21 before the taxpayer actually receives like-kind replacement property. If the taxpayer  
22 actually or constructively receives money or property which does not meet the  
23 requirements of section 1031(a) in the full amount of the consideration for the  
24 relinquished property, the transaction will constitute a sale, and not a deferred  
25 exchange, even though the taxpayer may ultimately receive like-kind replacement  
26 property. For purposes of this section, property which does not meet the requirements  
27 of section 1031(a) (whether by being described in section 1031(a)(2) or otherwise) is  
28 referred to as "other property." For rules regarding actual and constructive receipt,  
29 and safe harbors therefrom, see paragraphs (f) and (g), respectively, of this section. For  
30 rules regarding the determination of gain or loss recognized and the basis of property  
31 received in a deferred exchange, see paragraph (j) of this section.

32

33 (b) Identification and receipt requirements –

34

35 (1) In general.

36

37 In the case of a deferred exchange, any replacement property received by the taxpayer  
38 will be treated as property which is not of a like kind to the relinquished property if --

39

40 (i) The replacement property is not "identified" before the end of the "identification  
41 period," or

42

43 (ii) The identified replacement property is not received before the end of the "exchange  
44 period."

45

46 (2) Identification period and exchange period.

47



# EXETER

1031 Exchange Services LLC

1 (i) The identification period begins on the date the taxpayer transfers the relinquished  
2 property and ends at midnight on the 45th day thereafter.

3  
4 (ii) The exchange period begins on the date the taxpayer transfers the relinquished  
5 property and ends at midnight on the earlier of the 180th day thereafter or the due  
6 date (including extensions) for the taxpayer's return of the tax imposed by chapter 1 of  
7 subtitle A of the Code for the taxable year in which the transfer of the relinquished  
8 property occurs.

9  
10 (iii) If, as part of the same deferred exchange, the taxpayer transfers more than one  
11 relinquished property and the relinquished properties are transferred on different  
12 dates, the identification period and the exchange period are determined by reference to  
13 the earliest date on which any of the properties are transferred.

14  
15 (iv) For purposes of this paragraph (b)(2), property is transferred when the property is  
16 disposed of within the meaning of section 1001(a).

17  
18 (3) Example.

19  
20 This paragraph (b) may be illustrated by the following example.

21  
22 Example. (i) M is a corporation that files its Federal income tax return on a calendar  
23 year basis. M and C enter into an agreement for an exchange of property that requires  
24 M to transfer property X to C. Under the agreement, M is to identify like-kind  
25 replacement property which C is required to purchase and to transfer to M. M  
26 transfers property X to C on November 16, 1992.

27  
28 (ii) The identification period ends at midnight on December 31, 1992, the day which is  
29 45 days after the date of transfer of property X. The exchange period ends at midnight  
30 on March 15, 1993, the due date for M's Federal income tax return for the taxable year  
31 in which M transferred property X. However, if M is allowed the automatic six-month  
32 extension for filing its tax return, the exchange period ends at midnight on May 15,  
33 1993, the day which is 180 days after the date of transfer of property X.

34  
35 (c) Identification of replacement property before the end of the identification period –

36  
37 (1) In general.

38  
39 For purposes of paragraph (b)(1)(i) of this section (relating to the identification  
40 requirement), replacement property is identified before the end of the identification  
41 period only if the requirements of this paragraph (c) are satisfied with respect to the  
42 replacement property. However, any replacement property that is received by the  
43 taxpayer before the end of the identification period will in all events be treated as  
44 identified before the end of the identification period.

45  
46 (2) Manner of identifying replacement property.

47



# EXETER

1031 Exchange Services LLC

1 Replacement property is identified only if it is designated as replacement property in a  
2 written document signed by the taxpayer and hand delivered, mailed, telecopied, or  
3 otherwise sent before the end of the identification period to either --

4  
5 (i) The person obligated to transfer the replacement property to the taxpayer  
6 (regardless of whether that person is a disqualified person as defined in paragraph (k)  
7 of this section); or

8  
9 (ii) Any other person involved in the exchange other than the taxpayer or a disqualified  
10 person (as defined in paragraph (k) of this section).

11  
12 Examples of persons involved in the exchange include any of the parties to the  
13 exchange, an intermediary, an escrow agent, and a title company. An identification of  
14 replacement property made in a written agreement for the exchange of properties  
15 signed by all parties thereto before the end of the identification period will be treated  
16 as satisfying the requirements of this paragraph (c)(2).

17  
18 (3) Description of replacement property.

19  
20 Replacement property is identified only if it is unambiguously described in the written  
21 document or agreement. Real property generally is unambiguously described if it is  
22 described by a legal description, street address, or distinguishable name (e.g., the  
23 Mayfair Apartment Building). Personal property generally is unambiguously described  
24 if it is described by a specific description of the particular type of property. For  
25 example, a truck generally is unambiguously described if it is described by a specific  
26 make, model, and year.

27  
28 (4) Alternative and multiple properties.

29  
30 (i) The taxpayer may identify more than one replacement property. Regardless of the  
31 number of relinquished properties transferred by the taxpayer as part of the same  
32 deferred exchange, the maximum number of replacement properties that the taxpayer  
33 may identify is --

34  
35 (A) Three properties without regard to the fair market values of the properties (the "3-  
36 property rule"), or

37  
38 (B) Any number of properties as long as their aggregate fair market value as of the end  
39 of the identification period does not exceed 200 percent of the aggregate fair market  
40 value of all the relinquished properties as of the date the relinquished properties were  
41 transferred by the taxpayer (the "200-percent rule").

42  
43 (ii) If, as of the end of the identification period, the taxpayer has identified more  
44 properties as replacement properties than permitted by paragraph (c)(4)(i) of this  
45 section, the taxpayer is treated as if no replacement property had been identified. The  
46 preceding sentence will not apply, however, and an identification satisfying the  
47 requirements of paragraph (c)(4)(i) of this section will be considered made, with respect



# EXETER

1031 Exchange Services LLC

1 to --

2

3 (A) Any replacement property received by the taxpayer before the end of the  
4 identification period, and

5

6 (B) Any replacement property identified before the end of the identification period and  
7 received before the end of the exchange period, but only if the taxpayer receives before  
8 the end of the exchange period identified replacement property the fair market value of  
9 which is at least 95 percent of the aggregate fair market value of all identified  
10 replacement properties (the "95-percent rule").

11

12 For this purpose, the fair market value of each identified replacement property is  
13 determined as of the earlier of the date the property is received by the taxpayer or the  
14 last day of the exchange period.

15

16 (iii) For purposes of applying the 3-property rule, the 200-percent rule, and the 95-  
17 percent rule, all identifications of replacement property, other than identifications of  
18 replacement property that have been revoked in the manner provided in paragraph  
19 (c)(6) of this section, are taken into account. For example, if, in a deferred exchange, B  
20 transfers property X with a fair market value of \$ 100,000 to C and B receives like-  
21 kind property Y with a fair market value of \$ 50,000 before the end of the  
22 identification period, under paragraph (c)(1) of this section, property Y is treated as  
23 identified by reason of being received before the end of the identification period. Thus,  
24 under paragraph (c)(4)(i) of this section, B may identify either two additional  
25 replacement properties of any fair market value or any number of additional  
26 replacement properties as long as the aggregate fair market value of the additional  
27 replacement properties does not exceed \$ 150,000.

28

29 (5) Incidental property disregarded. (i) Solely for purposes of applying this paragraph  
30 (c), property that is incidental to a larger item of property is not treated as property  
31 that is separate from the larger item of property. Property is incidental to a larger item  
32 of property if --

33

34 (A) In standard commercial transactions, the property is typically transferred together  
35 with the larger item of property, and

36

37 (B) The aggregate fair market value of all of the incidental property does not exceed 15  
38 percent of the aggregate fair market value of the larger item of property.

39

40 (ii) This paragraph (c)(5) may be illustrated by the following examples.

41

42 Example 1. For purposes of paragraph (c) of this section, a spare tire and tool kit will  
43 not be treated as separate property from a truck with a fair market value of \$ 10,000,  
44 if the aggregate fair market value of the spare tire and tool kit does not exceed \$ 1,500.  
45 For purposes of the 3-property rule, the truck, spare tire, and tool kit are treated as 1  
46 property. Moreover, for purposes of paragraph (c)(3) of this section (relating to the  
47 description of replacement property), the truck, spare tire, and tool kit are all



# EXETER

1031 Exchange Services LLC

1 considered to be unambiguously described if the make, model, and year of the truck  
2 are specified, even if no reference is made to the spare tire and tool kit.

3  
4 Example 2. For purposes of paragraph (c) of this section, furniture, laundry machines,  
5 and other miscellaneous items of personal property will not be treated as separate  
6 property from an apartment building with a fair market value of \$ 1,000,000, if the  
7 aggregate fair market value of the furniture, laundry machines, and other personal  
8 property does not exceed \$ 150,000. For purposes of the 3-property rule, the  
9 apartment building, furniture, laundry machines, and other personal property are  
10 treated as 1 property. Moreover, for purposes of paragraph (c)(3) of this section  
11 (relating to the description of replacement property), the apartment building, furniture,  
12 laundry machines, and other personal property are all considered to be  
13 unambiguously described if the legal description, street address, or distinguishable  
14 name of the apartment building is specified, even if no reference is made to the  
15 furniture, laundry machines, and other personal property.

16  
17 (6) Revocation of identification.

18  
19 An identification of replacement property may be revoked at any time before the end of  
20 the identification period. An identification of replacement property is revoked only if  
21 the revocation is made in a written document signed by the taxpayer and hand  
22 delivered, mailed, telecopied, or otherwise sent before the end of the identification  
23 period to the person to whom the identification of the replacement property was sent.  
24 An identification of replacement property that is made in a written agreement for the  
25 exchange of properties is treated as revoked only if the revocation is made in a written  
26 amendment to the agreement or in a written document signed by the taxpayer and  
27 hand delivered, mailed, telecopied, or otherwise sent before the end of the identification  
28 period to all of the parties to the agreement.

29  
30 (7) Examples.

31  
32 This paragraph (c) may be illustrated by the following examples.

33  
34 Unless otherwise provided in an example, the following facts are assumed: B, a  
35 calendar year taxpayer, and C agree to enter into a deferred exchange. Pursuant to  
36 their agreement, B transfers real property X to C on May 17, 1991. Real property X,  
37 which has been held by B for investment, is unencumbered and has a fair market  
38 value on May 17, 1991, of \$ 100,000. On or before July 1, 1991 (the end of the  
39 identification period), B is to identify replacement property that is of a like kind to real  
40 property X. On or before November 13, 1991 (the end of the exchange period), C is  
41 required to purchase the property identified by B and to transfer that property to B. To  
42 the extent the fair market value of the replacement property transferred to B is greater  
43 or less than the fair market value of real property X, either B or C, as applicable, will  
44 make up the difference by paying cash to the other party after the date the  
45 replacement property is received by B. No replacement property is identified in the  
46 agreement. When subsequently identified, the replacement property is described by  
47 legal description and is of a like kind to real property X (determined without regard to



# EXETER

1031 Exchange Services LLC

1 section 1031(a)(3) and this section). B intends to hold the replacement property  
2 received for investment.

3  
4 Example 1. (i) On July 2, 1991, B identifies real property E as replacement property by  
5 designating real property E as replacement property in a written document signed by  
6 B and personally delivered to C.

7  
8 (ii) Because the identification was made after the end of the identification period,  
9 pursuant to paragraph (b)(1)(i) of this section (relating to the identification  
10 requirement), real property E is treated as property which is not of a like kind to real  
11 property X.

12  
13 Example 2. (i) C is a corporation of which 20 percent of the outstanding stock is owned  
14 by B. On July 1, 1991, B identifies real property F as replacement property by  
15 designating real property F as replacement property in a written document signed by B  
16 and mailed to C.

17  
18 (ii) Because C is the person obligated to transfer the replacement property to B, real  
19 property F is identified before the end of the identification period. The fact that C is a  
20 "disqualified person" as defined in paragraph (k) of this section does not change this  
21 result.

22  
23 (iii) Real property F would also have been treated as identified before the end of the  
24 identification period if, instead of sending the identification to C, B had designated real  
25 property F as replacement property in a written agreement for the exchange of  
26 properties signed by all parties thereto on or before July 1, 1991.

27  
28 Example 3. (i) On June 3, 1991, B identifies the replacement property as "unimproved  
29 land located in Hood County with a fair market value not to exceed \$ 100,000." The  
30 designation is made in a written document signed by B and personally delivered to C.  
31 On July 8, 1991, B and C agree that real property G is the property described in the  
32 June 3, 1991 document.

33  
34 (ii) Because real property G was not unambiguously described before the end of the  
35 identification period, no replacement property is identified before the end of the  
36 identification period.

37  
38 Example 4. (i) On June 28, 1991, B identifies real properties H, J, and K as  
39 replacement properties by designating these properties as replacement properties in a  
40 written document signed by B and personally delivered to C. The written document  
41 provides that by August 1, 1991, B will orally inform C which of the identified  
42 properties C is to transfer to B. As of July 1, 1991, the fair market values of real  
43 properties H, J, and K are \$ 75,000, \$ 100,000, and \$ 125,000, respectively.

44  
45 (ii) Because B did not identify more than three properties as replacement properties,  
46 the requirements of the 3-property rule are satisfied, and real properties H, J, and K  
47 are all identified before the end of the identification period.





# EXETER

1031 Exchange Services LLC

1  
2 Example 5. (i) On May 17, 1991, B identifies real properties L, M, N, and P as  
3 replacement properties by designating these properties as replacement properties in a  
4 written document signed by B and personally delivered to C. The written document  
5 provides that by July 2, 1991, B will orally inform C which of the identified properties  
6 C is to transfer to B. As of July 1, 1991, the fair market values of real properties L, M,  
7 N, and P are \$ 30,000, \$ 40,000, \$ 50,000, and \$ 60,000, respectively.  
8

9 (ii) Although B identified more than three properties as replacement properties, the  
10 aggregate fair market value of the identified properties as of the end of the  
11 identification period (\$ 180,000) did not exceed 200 percent of the aggregate fair  
12 market value of real property X (200% X \$ 100,000=\$ 200,000). Therefore, the  
13 requirements of the 200-percent rule are satisfied, and real properties L, M, N, and P  
14 are all identified before the end of the identification period.  
15

16 Example 6. (i) On June 21, 1991, B identifies real properties Q, R, and S as  
17 replacement properties by designating these properties as replacement properties in a  
18 written document signed by B and mailed to C. On June 24, 1991, B identifies real  
19 properties T and U as replacement properties in a written document signed by B and  
20 mailed to C. On June 28, 1991, B revokes the identification of real properties Q and R  
21 in a written document signed by B and personally delivered to C.  
22

23 (ii) B has revoked the identification of real properties Q and R in the manner provided  
24 by paragraph (c)(6) of this section. Identifications of replacement property that have  
25 been revoked in the manner provided by paragraph (c)(6) of this section are not taken  
26 into account for purposes of applying the 3-property rule. Thus, as of June 28, 1991,  
27 B has identified only replacement properties S, T, and U for purposes of the 3-property  
28 rule. Because B did not identify more than three properties as replacement properties  
29 for purposes of the 3-property rule, the requirements of that rule are satisfied, and  
30 real properties S, T, and U are all identified before the end of the identification period.  
31

32 Example 7. (i) On May 20, 1991, B identifies real properties V and W as replacement  
33 properties by designating these properties as replacement properties in a written  
34 document signed by B and personally delivered to C. On June 4, 1991, B identifies  
35 real properties Y and Z as replacement properties in the same manner. On June 5,  
36 1991, B telephones C and orally revokes the identification of real properties V and W.  
37 As of July 1, 1991, the fair market values of real properties V, W, Y, and Z are \$  
38 50,000, \$ 70,000, \$ 90,000, and \$ 100,000, respectively. On July 31, 1991, C  
39 purchases real property Y and Z and transfers them to B.  
40

41 (ii) Pursuant to paragraph (c)(6) of this section (relating to revocation of identification),  
42 the oral revocation of the identification of real properties V and W is invalid. Thus, the  
43 identification of real properties V and W is taken into account for purposes of  
44 determining whether the requirements of paragraph (c)(4) of this section (relating to  
45 the identification of alternative and multiple properties) are satisfied. Because B  
46 identified more than three properties and the aggregate fair market value of the  
47 identified properties as of the end of the identification period (\$ 310,000) exceeds 200



# EXETER

1031 Exchange Services LLC

1 percent of the fair market value of real property X ( $200\% \times \$ 100,000 = \$ 200,000$ ),  
2 the requirements of paragraph (c)(4) of this section are not satisfied, and B is treated  
3 as if B did not identify any replacement property.  
4

5 (d) Receipt of identified replacement property -- (1) In general. For purposes of  
6 paragraph (b)(1)(ii) of this section (relating to the receipt requirement), the identified  
7 replacement property is received before the end of the exchange period only if the  
8 requirements of this paragraph (d) are satisfied with respect to the replacement  
9 property. In the case of a deferred exchange, the identified replacement property is  
10 received before the end of the exchange period if --  
11

12 (i) The taxpayer receives the replacement property before the end of the exchange  
13 period, and  
14

15 (ii) The replacement property received is substantially the same property as identified.  
16

17 If the taxpayer has identified more than one replacement property, section  
18 1031(a)(3)(B) and this paragraph (d) are applied separately to each replacement  
19 property.  
20

21 (2) Examples. This paragraph (d) may be illustrated by the following examples. The  
22 following facts are assumed: B, a calendar year taxpayer, and C agree to enter into a  
23 deferred exchange. Pursuant to their agreement, B transfers real property X to C on  
24 May 17, 1991. Real property X, which has been held by B for investment, is  
25 unencumbered and has a fair market value on May 17, 1991, of \$ 100,000. On or  
26 before July 1, 1991 (the end of the identification period), B is to identify replacement  
27 property that is of a like kind to real property X. On or before November 13, 1991 (the  
28 end of the exchange period), C is required to purchase the property identified by B and  
29 to transfer that property to B. To the extent the fair market value of the replacement  
30 property transferred to B is greater or less than the fair market value of real property  
31 X, either B or C, as applicable, will make up the difference by paying cash to the other  
32 party after the date the replacement property is received by B. The replacement  
33 property is identified in a manner that satisfies paragraph (c) of this section (relating  
34 to identification of replacement property) and is of a like kind to real property X  
35 (determined without regard to section 1031(a)(3) and this section). B intends to hold  
36 any replacement property received for investment.  
37

38 Example 1. (i) In the agreement, B identifies real properties J, K, and L as replacement  
39 properties. The agreement provides that by July 26, 1991, B will orally inform C which  
40 of the properties C is to transfer to B.  
41

42 (ii) As of July 1, 1991, the fair market values of real properties J, K, and L are \$  
43 75,000, \$ 100,000, and \$ 125,000, respectively. On July 26, 1991, B instructs C to  
44 acquire real property K. On October 31, 1991, C purchases real property K for \$  
45 100,000 and transfers the property to B.  
46

47 (iii) Because real property K was identified before the end of the identification period



# EXETER

1031 Exchange Services LLC

1 and was received before the end of the exchange period, the identification and receipt  
2 requirements of section 1031(a)(3) and this section are satisfied with respect to real  
3 property K.

4  
5 Example 2. (i) In the agreement, B identifies real property P as replacement property.  
6 Real property P consists of two acres of unimproved land. On October 15, 1991, the  
7 owner of real property P erects a fence on the property. On November 1, 1991, C  
8 purchases real property P and transfers it to B.

9  
10 (ii) The erection of the fence on real property P subsequent to its identification did not  
11 alter the basic nature or character of real property P as unimproved land. B is  
12 considered to have received substantially the same property as identified.

13  
14 Example 3. (i) In the agreement, B identifies real property Q as replacement property.  
15 Real property Q consists of a barn on two acres of land and has a fair market value of  
16 \$ 250,000 (\$ 187,500 for the barn and underlying land and \$ 87,500 for the  
17 remaining land). As of July 26, 1991, real property Q remains unchanged and has a  
18 fair market value of \$ 250,000. On that date, at B's direction, C purchases the barn  
19 and underlying land for \$ 187,500 and transfers it to B, and B pays \$ 87,500 to C.

20  
21 (ii) The barn and underlying land differ in basic nature or character from real property  
22 Q as a whole, B is not considered to have received substantially the same property as  
23 identified.

24  
25 Example 4. (i) In the agreement, B identifies real property R as replacement property.  
26 Real property R consists of two acres of unimproved land and has a fair market value  
27 of \$ 250,000. As of October 3, 1991, real property R remains unimproved and has a  
28 fair market value of \$ 250,000. On that date, at B's direction, C purchases 1 1/2 acres  
29 of real property R for \$ 187,500 and transfers it to B, and B pays \$ 87,500 to C.

30  
31 (ii) The portion of real property R that B received does not differ from the basic nature  
32 or character of real property R as a whole. Moreover, the fair market value of the  
33 portion of real property R that B received (\$ 187,500) is 75 percent of the fair market  
34 value of real property R as of the date of receipt. Accordingly, B is considered to have  
35 received substantially the same property as identified.

36  
37 (e) Special rules for identification and receipt of replacement property to be produced –

38  
39 (1) In general.

40  
41 A transfer of relinquished property in a deferred exchange will not fail to qualify for  
42 nonrecognition of gain or loss under section 1031 merely because the replacement  
43 property is not in existence or is being produced at the time the property is identified  
44 as replacement property. For purposes of this paragraph (e), the terms "produced" and  
45 "production" have the same meanings as provided in section 263A(g)(1) and the  
46 regulations thereunder.



# EXETER

1031 Exchange Services LLC

1

2 (2) Identification of replacement property to be produced.

3

4 (i) In the case of replacement property that is to be produced, the replacement  
5 property must be identified as provided in paragraph (c) of this section (relating to  
6 identification of replacement property). For example, if the identified replacement  
7 property consists of improved real property where the improvements are to be  
8 constructed, the description of the replacement property satisfies the requirements of  
9 paragraph (c)(3) of this section (relating to description of replacement property) if a  
10 legal description is provided for the underlying land and as much detail is provided  
11 regarding construction of the improvements as is practicable at the time the  
12 identification is made.

13

14 (ii) For purposes of paragraphs (c)(4)(i)(B) and (c)(5) of this section (relating to the 200-  
15 percent rule and incidental property), the fair market value of replacement property  
16 that is to be produced is its estimated fair market value as of the date it is expected to  
17 be received by the taxpayer.

18

19 (3) Receipt of replacement property to be produced.

20

21 (i) For purposes of paragraph (d)(1)(ii) of this section (relating to receipt of the identified  
22 replacement property), in determining whether the replacement property received by  
23 the taxpayer is substantially the same property as identified where the identified  
24 replacement property is property to be produced, variations due to usual or typical  
25 production changes are not taken into account. However, if substantial changes are  
26 made in the property to be produced, the replacement property received will not be  
27 considered to be substantially the same property as identified.

28

29 (ii) If the identified replacement property is personal property to be produced, the  
30 replacement property received will not be considered to be substantially the same  
31 property as identified unless production of the replacement property received is  
32 completed on or before the date the property is received by the taxpayer.

33

34 (iii) If the identified replacement property is real property to be produced and the  
35 production of the property is not completed on or before the date the taxpayer receives  
36 the property, the property received will be considered to be substantially the same  
37 property as identified only if, had production been completed on or before the date the  
38 taxpayer receives the replacement property, the property received would have been  
39 considered to be substantially the same property as identified. Even so, the property  
40 received is considered to be substantially the same property as identified only to the  
41 extent the property received constitutes real property under local law.

42

43 (4) Additional rules.

44

45 The transfer of relinquished property is not within the provisions of section 1031(a) if  
46 the relinquished property is transferred in exchange for services (including production  
47 services). Thus, any additional production occurring with respect to the replacement



# EXETER

1031 Exchange Services LLC

1 property after the property is received by the taxpayer will not be treated as the receipt  
2 of property of a like kind.

3  
4 (5) Example.

5  
6 This paragraph (e) may be illustrated by the following example.

7  
8 Example. (i) B, a calendar year taxpayer, and C agree to enter into a deferred  
9 exchange. Pursuant to their agreement, B transfers improved real property X and  
10 personal property Y to C on May 17, 1991. On or before November 13, 1991 (the end  
11 of the exchange period), C is required to transfer to B real property M, on which C is  
12 constructing improvements, and personal property N, which C is producing. C is  
13 obligated to complete the improvements and production regardless of when properties  
14 M and N are transferred to B. Properties M and N are identified in a manner that  
15 satisfies paragraphs (c) (relating to identification of replacement property) and (e)(2) of  
16 this section. In addition, properties M and N are of a like kind, respectively, to real  
17 property X and personal property Y (determined without regard to section 1031(a)(3)  
18 and this section). On November 13, 1991, when construction of the improvements to  
19 property M is 20 percent completed and the production of property N is 90 percent  
20 completed, C transfers to B property M and property N. If construction of the  
21 improvements had been completed, property M would have been considered to be  
22 substantially the same property as identified. Under local law, property M constitutes  
23 real property to the extent of the underlying land and the 20 percent of the  
24 construction that is completed.

25  
26 (ii) Because property N is personal property to be produced and production of property  
27 N is not completed before the date the property is received by B, property N is not  
28 considered to be substantially the same property as identified and is treated as  
29 property which is not of a like kind to property Y.

30  
31 (iii) Property M is considered to be substantially the same property as identified to the  
32 extent of the underlying land and the 20 percent of the construction that is completed  
33 when property M is received by B. However, any additional construction performed by  
34 C with respect to property M after November 13, 1991, is not treated as the receipt of  
35 property of a like kind.

36  
37 (f) Receipt of money or other property –

38  
39 (1) In general.

40  
41 A transfer of relinquished property in a deferred exchange is not within the provisions  
42 of section 1031(a) if, as part of the consideration, the taxpayer receives money or other  
43 property. However, such a transfer, if otherwise qualified, will be within the provisions  
44 of either section 1031 (b) or (c). See § 1031(a)-1(a)(2). In addition, in the case of a  
45 transfer of relinquished property in a deferred exchange, gain or loss may be  
46 recognized if the taxpayer actually or constructively receives money or other property  
47 before the taxpayer actually receives like-kind replacement property. If the taxpayer





# EXETER

1031 Exchange Services LLC

1 actually or constructively receives money or other property in the full amount of the  
2 consideration for the relinquished property before the taxpayer actually receives like-  
3 kind replacement property, the transaction will constitute a sale and not a deferred  
4 exchange, even though the taxpayer may ultimately receive like-kind replacement  
5 property.

6  
7 (2) Actual and constructive receipt.

8  
9 Except as provided in paragraph (g) of this section (relating to safe harbors), for  
10 purposes of section 1031 and this section, the determination of whether (or the extent  
11 to which) the taxpayer is in actual or constructive receipt of money or other property  
12 before the taxpayer actually receives like-kind replacement property is made under the  
13 general rules concerning actual and constructive receipt and without regard to the  
14 taxpayer's method of accounting. The taxpayer is in actual receipt of money or  
15 property at the time the taxpayer actually receives the money or property or receives  
16 the economic benefit of the money or property. The taxpayer is in constructive receipt  
17 of money or property at the time the money or property is credited to the taxpayer's  
18 account, set apart for the taxpayer, or otherwise made available so that the taxpayer  
19 may draw upon it at any time or so that the taxpayer can draw upon it if notice of  
20 intention to draw is given. Although the taxpayer is not in constructive receipt of  
21 money or property if the taxpayer's control of its receipt is subject to substantial  
22 limitations or restrictions, the taxpayer is in constructive receipt of the money or  
23 property at the time the limitations or restrictions lapse, expire, or are waived. In  
24 addition, actual or constructive receipt of money or property by an agent of the  
25 taxpayer (determined without regard to paragraph (k) of this section) is actual or  
26 constructive receipt by the taxpayer.

27  
28 (3) Example.

29  
30 This paragraph (f) may be illustrated by the following example.

31  
32 Example. (i) B, a calendar year taxpayer, and C agree to enter into a deferred  
33 exchange. Pursuant to the agreement, on May 17, 1991, B transfers real property X to  
34 C. Real property X, which has been held by B for investment, is unencumbered and  
35 has a fair market value on May 17, 1991, of \$ 100,000. On or before July 1, 1991 (the  
36 end of the identification period), B is to identify replacement property that is of a like  
37 kind to real property X. On or before November 13, 1991 (the end of the exchange  
38 period), C is required to purchase the property identified by B and to transfer that  
39 property to B. At any time after May 17, 1991, and before C has purchased the  
40 replacement property, B has the right, upon notice, to demand that C pay \$ 100,000  
41 in lieu of acquiring and transferring the replacement property. Pursuant to the  
42 agreement, B identifies replacement property, and C purchases the replacement  
43 property and transfers it to B.

44  
45 (ii) Under the agreement, B has the unrestricted right to demand the payment of \$  
46 100,000 as of May 17, 1991. B is therefore in constructive receipt of \$ 100,000 on that  
47 date. Because B is in constructive receipt of money in the full amount of the





# EXETER

1031 Exchange Services LLC

1 consideration for the relinquished property before B actually receives the like-kind  
2 replacement property, the transaction constitutes a sale, and the transfer of real  
3 property X does not qualify for nonrecognition of gain or loss under section 1031. B is  
4 treated as if B received the \$ 100,000 in consideration for the sale of real property X  
5 and then purchased the like-kind replacement property.

6  
7 (iii) If B's right to demand payment of the \$ 100,000 were subject to a substantial  
8 limitation or restriction (e.g., the agreement provided that B had no right to demand  
9 payment before November 14, 1991 (the end of the exchange period)), then, for  
10 purposes of this section, B would not be in actual or constructive receipt of the money  
11 unless (or until) the limitation or restriction lapsed, expired, or was waived.

12  
13 (g) Safe harbors –

14  
15 (1) In general.

16  
17 Paragraphs (g)(2) through (g)(5) of this section set forth four safe harbors the use of  
18 which will result in a determination that the taxpayer is not in actual or constructive  
19 receipt of money or other property for purposes of section 1031 and this section. More  
20 than one safe harbor can be used in the same deferred exchange, but the terms and  
21 conditions of each must be separately satisfied. For purposes of the safe harbor rules,  
22 the term "taxpayer" does not include a person or entity utilized in a safe harbor (e.g., a  
23 qualified intermediary). See paragraph (g)(8), Example 3(v), of this section.

24  
25 (2) Security or guarantee arrangements.

26  
27 (i) In the case of a deferred exchange, the determination of whether the taxpayer is in  
28 actual or constructive receipt of money or other property before the taxpayer actually  
29 receives like-kind replacement property will be made without regard to the fact that  
30 the obligation of the taxpayer's transferee to transfer the replacement property to the  
31 taxpayer is or may be secured or guaranteed by one or more of the following --

32  
33 (A) A mortgage, deed of trust, or other security interest in property (other than cash or  
34 a cash equivalent),

35  
36 (B) A standby letter of credit which satisfies all of the requirements of § 15A.453-1  
37 (b)(3)(iii) and which may not be drawn upon in the absence of a default of the  
38 transferee's obligation to transfer like-kind replacement property to the taxpayer, or

39  
40 (C) A guarantee of a third party.

41  
42 (ii) Paragraph (g)(2)(i) of this section ceases to apply at the time the taxpayer has an  
43 immediate ability or unrestricted right to receive money or other property pursuant to  
44 the security or guarantee arrangement.

45  
46 (3) Qualified escrow accounts and qualified trusts.



# EXETER

1031 Exchange Services LLC

1 (i) In the case of a deferred exchange, the determination of whether the taxpayer is in  
2 actual or constructive receipt of money or other property before the taxpayer actually  
3 receives like-kind replacement property will be made without regard to the fact that  
4 the obligation of the taxpayer's transferee to transfer the replacement property to the  
5 taxpayer is or may be secured by cash or a cash equivalent if the cash or cash  
6 equivalent is held in a qualified escrow account or in a qualified trust.

7  
8 (ii) A qualified escrow account is an escrow account wherein --

9  
10 (A) The escrow holder is not the taxpayer or a disqualified person (as defined in  
11 paragraph (k) of this section), and

12  
13 (B) The escrow agreement expressly limits the taxpayer's rights to receive, pledge,  
14 borrow, or otherwise obtain the benefits of the cash or cash equivalent held in the  
15 escrow account as provided in paragraph (g)(6) of this section.

16  
17 (iii) A qualified trust is a trust wherein --

18  
19 (A) The trustee is not the taxpayer or a disqualified person (as defined in paragraph (k)  
20 of this section, except that for this purpose the relationship between the taxpayer and  
21 the trustee created by the qualified trust will not be considered a relationship under  
22 section 267(b)), and

23  
24 (B) The trust agreement expressly limits the taxpayer's rights to receive, pledge,  
25 borrow, or otherwise obtain the benefits of the cash or cash equivalent held by the  
26 trustee as provided in paragraph (g)(6) of this section.

27  
28 (iv) Paragraph (g)(3)(i) of this section ceases to apply at the time the taxpayer has an  
29 immediate ability or unrestricted right to receive, pledge, borrow, or otherwise obtain  
30 the benefits of the cash or cash equivalent held in the qualified escrow account or  
31 qualified trust. Rights conferred upon the taxpayer under state law to terminate or  
32 dismiss the escrow holder of a qualified escrow account or the trustee of a qualified  
33 trust are disregarded for this purpose.

34  
35 (v) A taxpayer may receive money or other property directly from a party to the  
36 exchange, but not from a qualified escrow account or a qualified trust, without  
37 affecting the application of paragraph (g)(3)(i) of this section.

38  
39 (4) Qualified intermediaries.

40  
41 (i) In the case of a taxpayer's transfer of relinquished property involving a qualified  
42 intermediary, the qualified intermediary is not considered the agent of the taxpayer for  
43 purposes of section 1031(a). In such a case, the taxpayer's transfer of relinquished  
44 property and subsequent receipt of like-kind replacement property is treated as an  
45 exchange, and the determination of whether the taxpayer is in actual or constructive  
46 receipt of money or other property before the taxpayer actually receives like-kind  
47 replacement property is made as if the qualified intermediary is not the agent of the



# EXETER

1031 Exchange Services LLC

1 taxpayer.

2

3 (ii) Paragraph (g)(4)(i) of this section applies only if the agreement between the taxpayer  
4 and the qualified intermediary expressly limits the taxpayer's rights to receive, pledge,  
5 borrow, or otherwise obtain the benefits of money or other property held by the  
6 qualified intermediary as provided in paragraph (g)(6) of this section.

7

8 (iii) A qualified intermediary is a person who --

9

10 (A) Is not the taxpayer or a disqualified person (as defined in paragraph (k) of this  
11 section), and

12

13 (B) Enters into a written agreement with the taxpayer (the "exchange agreement") and,  
14 as required by the exchange agreement, acquires the relinquished property from the  
15 taxpayer, transfers the relinquished property, acquires the replacement property, and  
16 transfers the replacement property to the taxpayer.

17

18 (iv) Regardless of whether an intermediary acquires and transfers property under  
19 general tax principals, solely for purposes of paragraph (g)(4)(iii)(B) of this section --

20

21 (A) An intermediary is treated as acquiring and transferring property if the  
22 intermediary acquires and transfers legal title to that property,

23

24 (b) An intermediary is treated as acquiring and transferring the relinquished property  
25 if the intermediary (either on its own behalf or as the agent of any party to the  
26 transaction) enters into an agreement with a person other than the taxpayer for the  
27 transfer of the relinquished property to that person and, pursuant to that agreement,  
28 the relinquished property is transferred to that person, and

29

30 (C) An intermediary is treated as acquiring and transferring replacement property if  
31 the intermediary (either on its own behalf or as the agent of any party to the  
32 transaction) enters into an agreement with the owner of the replacement property for  
33 the transfer of that property and, pursuant to that agreement, the replacement  
34 property is transferred to the taxpayer.

35

36 (v) Solely for purposes of paragraphs (g)(4)(iii) and (g)(4)(iv) of this section, an  
37 intermediary is treated as entering into an agreement if the rights of a party to the  
38 agreement are assigned to the intermediary and all parties to that agreement are  
39 notified in writing of the assignment on or before the date of the relevant transfer of  
40 property. For example, if a taxpayer enters into an agreement for the transfer of  
41 relinquished property and thereafter assigns its rights in that agreement to an  
42 intermediary and all parties to that agreement are notified in writing of the assignment  
43 on or before the date of the transfer of the relinquished property, the intermediary is  
44 treated as entering into that agreement. If the relinquished property is transferred  
45 pursuant to that agreement, the intermediary is treated as having acquired and  
46 transferred the relinquished property.

47



# EXETER

1031 Exchange Services LLC

1 (vi) Paragraph (g)(4)(i) of this section ceases to apply at the time the taxpayer has an  
2 immediate ability or unrestricted right to receive, pledge, borrow, or otherwise obtain  
3 the benefits of money or other property held by the qualified intermediary. Rights  
4 conferred upon the taxpayer under state law to terminate or dismiss the qualified  
5 intermediary are disregarded for this purpose.

6  
7 (vii) A taxpayer may receive money or other property directly from a party to the  
8 transaction other than the qualified intermediary without affecting the application of  
9 paragraph (g)(4)(i) of this section.

10  
11 (5) Interest and growth factors.

12  
13 In the case of a deferred exchange, the determination of whether the taxpayer is in  
14 actual or constructive receipt of money or other property before the taxpayer actually  
15 receives the like-kind replacement property will be made without regard to the fact  
16 that the taxpayer is or may be entitled to receive any interest or growth factor with  
17 respect to the deferred exchange. The preceding sentence applies only if the agreement  
18 pursuant to which the taxpayer is or may be entitled to the interest or growth factor  
19 expressly limits the taxpayer's rights to receive the interest or growth factor as  
20 provided in paragraph (g)(6) of this section. For additional rules concerning interest or  
21 growth factors, see paragraph (h) of this section.

22  
23 (6) Additional restrictions on safe harbors under paragraphs (g)(3) through (g)(5).

24  
25 (i) An agreement limits a taxpayer's rights as provided in this paragraph (g)(6) only if  
26 the agreement provides that the taxpayer has no rights, except as provided in  
27 paragraph (g)(6)(ii) and (g)(6)(iii) of this section, to receive, pledge, borrow, or otherwise  
28 obtain the benefits of money or other property before the end of the exchange period.

29  
30 (ii) The agreement may provide that if the taxpayer has not identified replacement  
31 property by the end of the identification period, the taxpayer may have rights to  
32 receive, pledge, borrow, or otherwise obtain the benefits of money or other property at  
33 any time after the end of the identification period.

34  
35 (iii) The agreement may provide that if the taxpayer has identified replacement  
36 property, the taxpayer may have rights to receive, pledge, borrow, or otherwise obtain  
37 the benefits of money or other property upon or after --

38  
39 (A) The receipt by the taxpayer of all of the replacement property to which the taxpayer  
40 is entitled under the exchange agreement, or

41  
42 (B) The occurrence after the end of the identification period of a material and  
43 substantial contingency that --

44  
45 (1) Relates to the deferred exchange,

46  
47 (2) Is provided for in writing, and



# EXETER

1031 Exchange Services LLC

1  
2 (3) Is beyond the control of the taxpayer and of any disqualified person (as defined in  
3 paragraph (k) of this section), other than the person obligated to transfer the  
4 replacement property to the taxpayer.

5  
6 (7) Items disregarded in applying safe harbors under paragraphs (g)(3) through (g)(5).  
7 In determining whether a safe harbor under paragraphs (g)(3) through (g)(5) of this  
8 section ceases to apply and whether the taxpayer's rights to receive, pledge, borrow, or  
9 otherwise obtain the benefits of money or other property are expressly limited as  
10 provided in paragraph (g)(6) of this section, the taxpayer's receipt of or right to receive  
11 any of the following items will be disregarded --

12  
13 (i) Items that a seller may receive as a consequence of the disposition of property and  
14 that are not included in the amount realized from the disposition of property (e.g.,  
15 prorated rents), and

16  
17 (ii) Transactional items that relate to the disposition of the relinquished property or to  
18 the acquisition of the replacement property and appear under local standards in the  
19 typical closing statements as the responsibility of a buyer or seller (e.g., commissions,  
20 prorated taxes, recording or transfer taxes, and title company fees).

21  
22 (8) Examples.

23  
24 This paragraph (g) may be illustrated by the following examples. Unless otherwise  
25 provided in an example, the following facts are assumed: B, a calendar year taxpayer,  
26 and C agree to enter into a deferred exchange. Pursuant to their agreement, B is to  
27 transfer real property X to C on May 17, 1991. Real property X, which has been held  
28 by B for investment, is unencumbered and has a fair market value on May 17, 1991,  
29 of \$ 100,000. On or before July 1, 1991 (the end of the identification period), B is to  
30 identify replacement property that is of a like kind to real property X. On or before  
31 November 13, 1991 (the end of the exchange period), C is required to purchase the  
32 property identified by B and to transfer that property to B. To the extent the fair  
33 market value of the replacement property transferred to B is greater or less than the  
34 fair market value property X, either B or C, as applicable, will make up the difference  
35 by paying cash to the other party after the date the replacement property is received  
36 by B. The replacement property is identified as provided in paragraph (c) of this  
37 section (relating to identification of replacement property) and is of a like kind to real  
38 property X (determined without regard to section 1031(a)(3) and this section). B  
39 intends to hold any replacement property received for investment.

40  
41 Example 1. (i) On May 17, 1991, B transfers real property X to C. On the same day, C  
42 pays \$ 10,000 to B and deposits \$ 90,000 in escrow as security for C's obligation to  
43 perform under the agreement. The escrow agreement provides that B has no rights to  
44 receive, pledge, borrow, or otherwise obtain the benefits of the money in escrow before  
45 November 14, 1991, except that:

46  
47 (A) if B fails to identify replacement property on or before July 1, 1991, B may demand



# EXETER

1031 Exchange Services LLC

1 the funds in escrow at any time after July 1, 1991; and

2

3 (B) if B identifies and receives replacement property, then B may demand the balance  
4 of the remaining funds in escrow at any time after B has received the replacement  
5 property.

6

7 The funds in escrow may be used to purchase the replacement property. The escrow  
8 holder is not a disqualified person as defined in paragraph (k) of this section. Pursuant  
9 to the terms of the agreement, B identifies replacement property, and C purchases the  
10 replacement property using the funds in escrow and transfers the replacement property  
11 to B.

12

13 (ii) C's obligation to transfer the replacement property to B was secured by cash held  
14 in a qualified escrow account because the escrow holder was not a disqualified person  
15 and the escrow agreement expressly limited B's rights to receive, pledge, borrow, or  
16 otherwise obtain the benefits of the money in escrow as provided in paragraph (g)(6) of  
17 this section. In addition, B did not have the immediate ability or unrestricted right to  
18 receive money or other property in escrow before B actually received the like-kind  
19 replacement property. Therefore, for purposes of section 1031 and this section, B is  
20 determined not to be in actual or constructive receipt of the \$ 90,000 held in escrow  
21 before B received the like-kind replacement property. The transfer of real property X  
22 by B and B's acquisition of the replacement property qualify as an exchange under  
23 section 1031. See paragraph (j) of this section for determining the amount of gain or  
24 loss recognized.

25

26 Example 2. (i) On May 17, 1991, B transfers real property X to C, and C deposits \$  
27 100,000 in escrow as security for C's obligation to perform under the agreement. Also  
28 on May 17, B identifies real property J as replacement property. The escrow agreement  
29 provides that no funds may be paid out without prior written approval of both B and  
30 C. The escrow agreement also provides that B has no rights to receive, pledge, borrow,  
31 or otherwise obtain the benefits of the money in escrow before November 14, 1991,  
32 except that:

33

34 (A) B may demand the funds in escrow at any time after the later of July 1, 1991, and  
35 the occurrence of any of the following events --

36

37 (1) real property J is destroyed, seized, requisitioned, or condemned, or

38

39 (2) a determination is made that the regulatory approval necessary for the transfer of  
40 real property J cannot be obtained in time for real property J to be transferred to B  
41 before the end of the exchange period;

42

43 (B) B may demand the funds in escrow at any time after August 14, 1991, if real  
44 property J has not been rezoned from residential to commercial use by that date; and

45

46 (C) B may demand the funds in escrow at the time B receives real property J or any  
47 time thereafter.





# EXETER

1031 Exchange Services LLC

1  
2 Otherwise, B is entitled to all funds in escrow after November 13, 1991. The funds in  
3 escrow may be used to purchase the replacement property. The escrow holder is not a  
4 disqualified person as described in paragraph (k) of this section. Real property J is not  
5 rezoned from residential to commercial use on or before August 14, 1991.

6  
7 (ii) C's obligation to transfer the replacement property to B was secured by cash held  
8 in a qualified escrow account because the escrow holder was not a disqualified person  
9 and the escrow agreement expressly limited B's rights to receive, pledge, borrow, or  
10 otherwise obtain the benefits of the money in escrow as provided in paragraph (g)(6) of  
11 this section. From May 17, 1991, until August 15, 1991, B did not have the immediate  
12 ability or unrestricted right to receive money or other property before B actually  
13 received the like-kind replacement property. Therefore, for purposes of section 1031  
14 and this section, B is determined not to be in actual or constructive receipt of the \$  
15 100,000 in escrow from May 17, 1991, until August 15, 1991. However, on August 15,  
16 1991, B had the unrestricted right, upon notice, to draw upon the \$ 100,000 held in  
17 escrow. Thus, the safe harbor ceased to apply and B was in constructive receipt of the  
18 funds held in escrow. Because B constructively received the full amount of the  
19 consideration (\$ 100,000) before B actually received the like-kind replacement  
20 property, the transaction is treated as a sale and not as a deferred exchange. The  
21 result does not change even if B chose not to demand the funds in escrow and  
22 continued to attempt to have real property J rezoned and to receive the property on or  
23 before November 13, 1991.

24  
25 (iii) If real property J had been rezoned on or before August 14, 1991, and C had  
26 purchased real property J and transferred it to B on or before November 13, 1991, the  
27 transaction would have qualified for nonrecognition of gain or loss under section  
28 1031(a).

29  
30 Example 3. (i) On May 1, 1991, D offers to purchase real property X for \$ 100,000.  
31 However, D is unwilling to participate in a like-kind exchange. B thus enters into an  
32 exchange agreement with C whereby B retains C to facilitate an exchange with respect  
33 to real property X. C is not a disqualified person as described in paragraph (k) of this  
34 section. The exchange agreement between B and C provides that B is to execute and  
35 deliver a deed conveying real property X to C who, in turn, is to execute and deliver a  
36 deed conveying real property X to D. The exchange agreement expressly limits B's  
37 rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other  
38 property held by C as provided in paragraph (g)(6) of this section. On May 3, 1991, C  
39 enters into an agreement with D to transfer real property X to D for \$ 100,000. On  
40 May 17, 1991, B executes and delivers to C a deed conveying real property X to C. On  
41 the same date, C executes and delivers to D a deed conveying real property X to D,  
42 and D deposits \$ 100,000 in escrow. The escrow holder is not a disqualified person as  
43 defined in paragraph (k) of this section and the escrow agreement expressly limits B's  
44 rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other  
45 property in escrow as provided in paragraph (g)(6) of this section. However, the escrow  
46 agreement provides that the money in escrow may be used to purchase replacement  
47 property. On June 3, 1991, B identifies real property K as replacement property. On



# EXETER

1031 Exchange Services LLC

1 August 9, 1991, E executes and delivers to C a deed conveying real property K to C  
2 and \$ 80,000 is released from the escrow and paid to E. On the same date, C executes  
3 and delivers to B a deed conveying real property K to B, and the escrow holder pays B  
4 \$ 20,000, the balance of the \$ 100,000 sale price of real property X remaining after the  
5 purchase of real property K for \$ 80,000.

6  
7 (ii) B and C entered into an exchange agreement that satisfied the requirements of  
8 paragraph (g)(4)(iii)(B) of this section. Regardless of whether C may have acquired and  
9 transferred real property X under general tax principles, C is treated as having  
10 acquired and transferred real property X because C acquired and transferred legal title  
11 to real property X. Similarly, C is treated as having acquired and transferred real  
12 property K because C acquired and transferred legal title to real property K. Thus, C  
13 was a qualified intermediary. This result is reached for purposes of this section  
14 regardless of whether C was B's agent under state law.

15  
16 (iii) Because the escrow holder was not a disqualified person and the escrow  
17 agreement expressly limited B's rights to receive, pledge, borrow, or otherwise obtain  
18 the benefits of money or other property in escrow as provided in paragraph (g)(6) of  
19 this section, the escrow account was a qualified escrow account. For purposes of  
20 section 1031 and this section, therefore, B is determined not to be in actual or  
21 constructive receipt of the funds in escrow before B received real property K.

22  
23 (iv) The exchange agreement between B and C expressly limited B's rights to receive,  
24 pledge, borrow, or otherwise obtain the benefits of any money held by C as provided in  
25 paragraph (g)(6) of this section. Because C was a qualified intermediary, for purposes  
26 of section 1031 and this section B is determined not to be in actual or constructive  
27 receipt of any funds held by C before B received real property K. In addition, B's  
28 transfer of real property X and acquisition of real property K qualify as an exchange  
29 under section 1031. See paragraph (j) of this section for determining the amount of  
30 gain or loss recognized.

31  
32 (v) If the escrow agreement had expressly limited C's rights to receive, pledge, borrow,  
33 or otherwise obtain the benefits of money or other property in escrow as provided in  
34 paragraph (g)(6) of this section, but had not expressly limited B's rights to receive,  
35 pledge, borrow, or otherwise obtain the benefits of that money or other property, the  
36 escrow account would not have been a qualified escrow account. Consequently,  
37 paragraph (g)(3)(i) of this section would not have been applicable in determining  
38 whether B was in actual or constructive receipt of that money or other property before  
39 B received real property K.

40  
41 Example 4. (i) On May 1, 1991, B enters into an agreement to sell real property X to D  
42 for \$ 100,000 on May 17, 1991. However, D is unwilling to participate in a like-kind  
43 exchange. B thus enters into an exchange agreement with C whereby B retains C to  
44 facilitate an exchange with respect to real property X. C is not a disqualified person as  
45 described in paragraph (k) of this section. In the exchange agreement between B and  
46 C, B assigns to C all of B's rights in the agreement with D. The exchange agreement  
47 expressly limits B's rights to receive, pledge, borrow, or otherwise obtain the benefits



# EXETER

1031 Exchange Services LLC

1 of money or other property held by C as provided in paragraph (g)(6) of this section.  
2 On May 17, 1991, B notifies D in writing of the assignment. On the same date, B  
3 executes and delivers to D a deed conveying real property X to D. D pays \$ 10,000 to B  
4 and \$ 90,000 to C. On June 1, 1991, B identifies real property L as replacement  
5 property. On July 5, 1991, B enters into an agreement to purchase real property L  
6 from E for \$ 90,000, assigns its rights in that agreement to C, and notifies E in writing  
7 of the assignment. On August 9, 1991, C pays \$ 90,000 to E, and E executes and  
8 delivers to B a deed conveying real property L to B.

9  
10 (ii) The exchange agreement entered into by B and C satisfied the requirements of  
11 paragraph (g)(4)(iii)(B) of this section. Because B's rights in its agreements with D and  
12 E were assigned to C, and D and E were notified in writing of the assignment on or  
13 before the transfer of real properties X and L, respectively, C is treated as entering into  
14 those agreements. Because C is treated as entering into an agreement with D for the  
15 transfer of real property X and, pursuant to that agreement, real property X was  
16 transferred to D, C is treated as acquiring and transferring real property X. Similarly,  
17 because C is treated as entering into an agreement with E for the transfer of real  
18 property K and, pursuant to that agreement, real property K was transferred to B, C is  
19 treated as acquiring and transferring real property K. This result is reached for  
20 purposes of this section regardless of whether C was B's agent under state law and  
21 regardless of whether C is considered, under general tax principles, to have acquired  
22 title or beneficial ownership of the properties. Thus, C was a qualified intermediary.

23  
24 (iii) The exchange agreement between B and C expressly limited B's rights to receive,  
25 pledge, borrow, or otherwise obtain the benefits of the money held by C as provided in  
26 paragraph (g)(6) of this section. Thus, B did not have the immediate ability or  
27 unrestricted right to receive money or other property held by C before B received real  
28 property L. For purposes of section 1031 and this section, therefore, B is determined  
29 not to be in actual or constructive receipt of the \$ 90,000 held by C before B received  
30 real property L. In addition, the transfer of real property X by B and B's acquisition of  
31 real property L qualify as an exchange under section 1031. See paragraph (j) of this  
32 section for determining the amount of gain or loss recognized.

33  
34 Example 5. (i) On May 1, 1991, B enters into an agreement to sell real property X to D  
35 for \$ 100,000. However, D is unwilling to participate in a like-kind exchange. B thus  
36 enters into an agreement with C whereby B retains C to facilitate an exchange with  
37 respect to real property X. C is not a disqualified person as described in paragraph (k)  
38 of this section. The agreement between B and C expressly limits B's rights to receive,  
39 pledge, borrow, or otherwise obtain the benefits of money or other property held by C  
40 as provided in paragraph (g)(6) of this section. C neither enters into an agreement with  
41 D to transfer real property X to D nor is assigned B's rights in B's agreement to sell  
42 real property X to D. On May 17, 1991, B transfers real property X to D and instructs  
43 D to transfer the \$ 100,000 to C. On June 1, 1991, B identifies real property M as  
44 replacement property. On August 9, 1991, C purchases real property L from E for \$  
45 100,000, and E executes and delivers to C a deed conveying real property M to C. On  
46 the same date, C executes and delivers to B a deed conveying real property M to B.

47



# EXETER

1031 Exchange Services LLC

1 (ii) Because B transferred real property X directly to D under B's agreement with D, C  
2 did not acquire real property X from B and transfer real property X to D. Moreover,  
3 because C did not acquire legal title to real property X, did not enter into an agreement  
4 with D to transfer real property X to D, and was not assigned B's rights in B's  
5 agreement to sell real property X to D, C is not treated as acquiring and transferring  
6 real property X. Thus, C was not a qualified intermediary and paragraph (g)(4)(i) of  
7 this section does not apply.

8  
9 (iii) B did not exchange real property X for real property M. Rather, B sold real  
10 property X to D and purchased, through C, real property M. Therefore, the transfer of  
11 real property X does not qualify for nonrecognition of gain or loss under section 1031.

12  
13 (h) Interest and growth factors –

14  
15 (1) In general.

16  
17 For purposes of this section, the taxpayer is treated as being entitled to receive  
18 interest or a growth factor with respect to a deferred exchange if the amount of money  
19 or property the taxpayer is entitled to receive depends upon the length of time elapsed  
20 between transfer of the relinquished property and receipt of the replacement property.

21  
22 (2) Treatment as interest.

23  
24 If, as part of a deferred exchange, the taxpayer receives interest or a growth factor, the  
25 interest or growth factor will be treated as interest, regardless of whether it is paid to  
26 the taxpayer in cash or in property (including property of a like kind). The taxpayer  
27 must include the interest or growth factor in income according to the taxpayer's  
28 method of accounting.

29  
30 (i) [Reserved]

31  
32 (j) Determination of gain or loss recognized and the basis of property received in a  
33 deferred exchange –

34  
35 (1) In general.

36  
37 Except as otherwise provided, the amount of gain or loss recognized and the basis of  
38 property received in a deferred exchange is determined by applying the rules of section  
39 1031 and the regulations thereunder. See §§ 1.1031(b)-1, 1.1031(c)-1, 1.1031(d)-1,  
40 1.1031(d)-1T, 1.1031(d)-2, and 1.1031(j)-1.

41  
42 (2) Coordination with section 453 –

43  
44 (i) Qualified escrow accounts and qualified trusts.

45  
46 Subject to the limitations of paragraphs (j)(2) (iv) and (v) of this section, in the case of a  
47 taxpayer's transfer of relinquished property in which the obligation of the taxpayer's



# EXETER

1031 Exchange Services LLC

1 transferee to transfer replacement property to the taxpayer is or may be secured by  
2 cash or a cash equivalent, the determination of whether the taxpayer has received a  
3 payment for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter will be  
4 made without regard to the fact that the obligation is or may be so secured if the cash  
5 or cash equivalent is held in a qualified escrow account or a qualified trust. This  
6 paragraph (j)(2)(i) ceases to apply at the earlier of --

7  
8 (A) The time described in paragraph (g)(3)(iv) of this section; or

9  
10 (B) The end of the exchange period.

11  
12 (ii) Qualified intermediaries. Subject to the limitations of paragraphs (j)(2) (iv) and (v) of  
13 this section, in the case of a taxpayer's transfer of relinquished property involving a  
14 qualified intermediary, the determination of whether the taxpayer has received a  
15 payment for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter is made as  
16 if the qualified intermediary is not the agent of the taxpayer. For purposes of this  
17 paragraph (j)(2)(ii), a person who otherwise satisfies the definition of a qualified  
18 intermediary is treated as a qualified intermediary even though that person ultimately  
19 fails to acquire identified replacement property and transfer it to the taxpayer. This  
20 paragraph (j)(2)(ii) ceases to apply at the earlier of --

21  
22 (A) The time described in paragraph (g)(4)(vi) of this section; or

23  
24 (B) The end of the exchange period.

25  
26 (iii) Transferee indebtedness. In the case of a transaction described in paragraph  
27 (j)(2)(ii) of this section, the receipt by the taxpayer of an evidence of indebtedness of the  
28 transferee of the qualified intermediary is treated as the receipt of an evidence of  
29 indebtedness of the person acquiring property from the taxpayer for purposes of  
30 section 453 and § 15a.453-1(b)(3)(i) of this chapter.

31  
32 (iv) Bona fide intent requirement. The provisions of paragraphs (j)(2) (i) and (ii) of this  
33 section do not apply unless the taxpayer has a bona fide intent to enter into a deferred  
34 exchange at the beginning of the exchange period. A taxpayer will be treated as having  
35 a bona fide intent only if it is reasonable to believe, based on all the facts and  
36 circumstances as of the beginning of the exchange period, that like-kind replacement  
37 property will be acquired before the end of the exchange period.

38  
39 (v) Disqualified property. The provisions of paragraphs (j)(2) (i) and (ii) of this section  
40 do not apply if the relinquished property is disqualified property. For purposes of this  
41 paragraph (j)(2), disqualified property means property that is not held for productive  
42 use in a trade or business or for investment or is property described in section  
43 1031(a)(2).

44  
45 (vi) Examples. This paragraph (j)(2) may be illustrated by the following examples.  
46 Unless otherwise provided in an example, the following facts are assumed: B is a  
47 calendar year taxpayer who agrees to enter into a deferred exchange. Pursuant to the





# EXETER

1031 Exchange Services LLC

1 agreement, B is to transfer real property X. Real property X, which has been held by B  
2 for investment, is unencumbered and has a fair market value of \$ 100,000 at the time  
3 of transfer. B's adjusted basis in real property X at that time is \$ 60,000. B identifies a  
4 single like-kind replacement property before the end of the identification period, and B  
5 receives the replacement property before the end of the exchange period. The  
6 transaction qualifies as a like-kind exchange under section 1031.  
7

8 Example 1. (i) On September 22, 1994, B transfers real property X to C and C agrees  
9 to acquire like-kind property and deliver it to B. On that date B has a bona fide intent  
10 to enter into a deferred exchange. C's obligation, which is not payable on demand or  
11 readily tradable, is secured by \$ 100,000 in cash. The \$ 100,000 is deposited by C in  
12 an escrow account that is a qualified escrow account under paragraph (g)(3) of this  
13 section. The escrow agreement provides that B has no rights to receive, pledge,  
14 borrow, or otherwise obtain the benefits of the cash deposited in the escrow account  
15 until the earlier of the date the replacement property is delivered to B or the end of the  
16 exchange period. On March 11, 1995, C acquires replacement property having a fair  
17 market value of \$ 80,000 and delivers the replacement property to B. The \$ 20,000 in  
18 cash remaining in the qualified escrow account is distributed to B at that time.  
19

20 (ii) Under section 1031(b), B recognizes gain to the extent of the \$ 20,000 in cash that  
21 B receives in the exchange. Under paragraph (j)(2)(i) of this section, the qualified  
22 escrow account is disregarded for purposes of section 453 and § 15a.453-1(b)(3)(i) of  
23 this chapter in determining whether B is in receipt of payment. Accordingly, B's  
24 receipt of C's obligation on September 22, 1994, does not constitute a payment.  
25 Instead, B is treated as receiving payment on March 11, 1995, on receipt of the \$  
26 20,000 in cash from the qualified escrow account. Subject to the other requirements of  
27 sections 453 and 453A, B may report the \$ 20,000 gain in 1995 under the installment  
28 method. See section 453(f)(6) for special rules for determining total contract price and  
29 gross profit in the case of an exchange described in section 1031(b).  
30

31 Example 2. (i) D offers to purchase real property X but is unwilling to participate in a  
32 like-kind exchange. B thus enters into an exchange agreement with C whereby B  
33 retains C to facilitate an exchange with respect to real property X. On September 22,  
34 1994, pursuant to the agreement, B transfers real property X to C who transfers it to  
35 D for \$ 100,000 in cash. On that date B has a bona fide intent to enter into a deferred  
36 exchange. C is a qualified intermediary under paragraph (g)(4) of this section. The  
37 exchange agreement provides that B has no rights to receive, pledge, borrow, or  
38 otherwise obtain the benefits of the money held by C until the earlier of the date the  
39 replacement property is delivered to B or the end of the exchange period. On March  
40 11, 1995, C acquires replacement property having a fair market value of \$ 80,000 and  
41 delivers it, along with the remaining \$ 20,000 from the transfer of real property X to B.  
42

43 (ii) Under section 1031(b), B recognizes gain to the extent of the \$ 20,000 cash B  
44 receives in the exchange. Under paragraph (j)(2)(ii) of this section, any agency  
45 relationship between B and C is disregarded for purposes of section 453 and §  
46 15a.453-1(b)(3)(i) of this chapter in determining whether B is in receipt of payment.  
47 Accordingly, B is not treated as having received payment on September 22, 1994, on





# EXETER

1031 Exchange Services LLC

1 C's receipt of payment from D for the relinquished property. Instead, B is treated as  
2 receiving payment on March 11, 1995, on receipt of the \$ 20,000 in cash from C.  
3 Subject to the other requirements of sections 453 and 453A, B may report the \$  
4 20,000 gain in 1995 under the installment method.

5  
6 Example 3. (i) D offers to purchase real property X but is unwilling to participate in a  
7 like-kind exchange. B enters into an exchange agreement with C whereby B retains C  
8 as a qualified intermediary to facilitate an exchange with respect to real property X.  
9 On December 1, 1994, pursuant to the agreement, B transfers real property X to C  
10 who transfers it to D for \$ 100,000 in cash. On that date B has a bona fide intent to  
11 enter into a deferred exchange. The exchange agreement provides that B has no rights  
12 to receive, pledge, borrow, or otherwise obtain the benefits of the cash held by C until  
13 the earliest of the end of the identification period if B has not identified replacement  
14 property, the date the replacement property is delivered to B, or the end of the  
15 exchange period. Although B has a bona fide intent to enter into a deferred exchange  
16 at the beginning of the exchange period, B does not identify or acquire any  
17 replacement property. In 1995, at the end of the identification period, C delivers the  
18 entire \$ 100,000 from the sale of real property X to B.

19  
20 (ii) Under section 1001, B realizes gain to the extent of the amount realized (\$ 100,000)  
21 over the adjusted basis in real property X (\$ 60,000), or \$ 40,000. Because B has a  
22 bona fide intent at the beginning of the exchange period to enter into a deferred  
23 exchange, paragraph (j)(2)(iv) of this section does not make paragraph (j)(2)(ii) of this  
24 section inapplicable even though B fails to acquire replacement property. Further,  
25 under paragraph (j)(2)(ii) of this section, C is a qualified intermediary even though C  
26 does not acquire and transfer replacement property to B. Thus, any agency  
27 relationship between B and C is disregarded for purposes of section 453 and §  
28 15a.453-1(b)(3)(i) of this chapter in determining whether B is in receipt of payment.  
29 Accordingly, B is not treated as having received payment on December 1, 1994, on C's  
30 receipt of payment from D for the relinquished property. Instead, B is treated as  
31 receiving payment at the end of the identification period in 1995 on receipt of the \$  
32 100,000 in cash from C. Subject to the other requirements of sections 453 and 453A,  
33 B may report the \$ 40,000 gain in 1995 under the installment method.

34  
35 Example 4. (i) D offers to purchase real property X but is unwilling to participate in a  
36 like-kind exchange. B thus enters into an exchange agreement with C whereby B  
37 retains C to facilitate an exchange with respect to real property X. C is a qualified  
38 intermediary under paragraph (g)(4) of this section. On September 22, 1994, pursuant  
39 to the agreement, B transfers real property X to C who then transfers it to D for \$  
40 80,000 in cash and D's 10-year installment obligation for \$ 20,000. On that date B  
41 has a bona fide intent to enter into a deferred exchange. The exchange agreement  
42 provides that B has no rights to receive, pledge, borrow, or otherwise obtain the  
43 benefits of the money or other property held by C until the earlier of the date the  
44 replacement property is delivered to B or the end of the exchange period. D's obligation  
45 bears adequate stated interest and is not payable on demand or readily tradable. On  
46 March 11, 1995, C acquires replacement property having a fair market value of \$  
47 80,000 and delivers it, along with the \$ 20,000 installment obligation, to B.



# EXETER

1031 Exchange Services LLC

1  
2 (ii) Under section 1031(b), \$ 20,000 of B's gain (i.e., the amount of the installment  
3 obligation B receives in the exchange) does not qualify for nonrecognition under  
4 section 1031(a). Under paragraphs (j)(2) (ii) and (iii) of this section, B's receipt of D's  
5 obligation is treated as the receipt of an obligation of the person acquiring the property  
6 for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter in determining  
7 whether B is in receipt of payment. Accordingly, B's receipt of the obligation is not  
8 treated as a payment. Subject to the other requirements of sections 453 and 453A, B  
9 may report the \$ 20,000 gain under the installment method on receiving payments  
10 from D on the obligation.

11  
12 Example 5. (i) B is a corporation that has held real property X to expand its  
13 manufacturing operations. However, at a meeting in November 1994, B's directors  
14 decide that real property X is not suitable for the planned expansion, and authorize a  
15 like-kind exchange of this property for property that would be suitable for the planned  
16 expansion. B enters into an exchange agreement with C whereby B retains C as a  
17 qualified intermediary to facilitate an exchange with respect to real property X. On  
18 November 28, 1994, pursuant to the agreement, B transfers real property X to C, who  
19 then transfers it to D for \$ 100,000 in cash. The exchange agreement does not include  
20 any limitations or conditions that make it unreasonable to believe that like-kind  
21 replacement property will be acquired before the end of the exchange period. The  
22 exchange agreement provides that B has no rights to receive, pledge, borrow, or  
23 otherwise obtain the benefits of the cash held by C until the earliest of the end of the  
24 identification period, if B has not identified replacement property, the date the  
25 replacement property is delivered to B, or the end of the exchange period. In early  
26 January 1995, B's directors meet and decide that it is not feasible to proceed with the  
27 planned expansion due to a business downturn reflected in B's preliminary financial  
28 reports for the last quarter of 1994. Thus, B's directors instruct C to stop seeking  
29 replacement property. C delivers the \$ 100,000 cash to B on January 12, 1995, at the  
30 end of the identification period. Both the decision to exchange real property X for other  
31 property and the decision to cease seeking replacement property because of B's  
32 business downturn are recorded in the minutes of the directors' meetings. There are  
33 no other facts or circumstances that would indicate whether, on November 28, 1994,  
34 B had a bona fide intent to enter into a deferred like-kind exchange.

35  
36 (ii) Under section 1001, B realizes gain to the extent of the amount realized (\$ 100,000)  
37 over the adjusted basis of real property X (\$ 60,000), or \$ 40,000. The directors'  
38 authorization of a like-kind exchange, the terms of the exchange agreement with C,  
39 and the absence of other relevant facts, indicate that B had a bona fide intent at the  
40 beginning of the exchange period to enter into a deferred like-kind exchange. Thus,  
41 paragraph (j)(2)(iv) of this section does not make paragraph (j)(2)(ii) of this section  
42 inapplicable, even though B fails to acquire replacement property. Further, under  
43 paragraph (j)(2)(ii) of this section, C is a qualified intermediary, even though C does not  
44 transfer replacement property to B. Thus, any agency relationship between B and C is  
45 disregarded for purposes of section 453 and § 15a.453-1(b)(3)(i) of this chapter in  
46 determining whether B is in receipt of payment. Accordingly, B is not treated as having  
47 received payment until January 12, 1995, on receipt of the \$ 100,000 cash from C.



# EXETER

1031 Exchange Services LLC

1 Subject to the other requirements of sections 453 and 453A, B may report the \$  
2 40,000 gain in 1995 under the installment method.

3  
4 Example 6. (i) B has held real property X for use in its trade or business, but decides  
5 to transfer that property because it is no longer suitable for B's planned expansion of  
6 its commercial enterprise. B and D agree to enter into a deferred exchange. Pursuant  
7 to their agreement, B transfers real property X to D on September 22, 1994, and D  
8 deposits \$ 100,000 cash in a qualified escrow account as security for D's obligation  
9 under the agreement to transfer replacement property to B before the end of the  
10 exchange period. D's obligation is not payable on demand or readily tradable. The  
11 agreement provides that B is not required to accept any property that is not zoned for  
12 commercial use. Before the end of the identification period, B identifies real properties  
13 J, K, and L, all zoned for residential use, as replacement properties. Any one of these  
14 properties, rezoned for commercial use, would be suitable for B's planned expansion.  
15 In recent years, the zoning board with jurisdiction over properties J, K, and L has  
16 rezoned similar properties for commercial use. The escrow agreement provides that B  
17 has no rights to receive, pledge, borrow, or otherwise obtain the benefits of the money  
18 in the escrow account until the earlier of the time that the zoning board determines,  
19 after the end of the identification period, that it will not rezone the properties for  
20 commercial use or the end of the exchange period. On January 5, 1995, the zoning  
21 board decides that none of the properties will be rezoned for commercial use. Pursuant  
22 to the exchange agreement, B receives the \$ 100,000 cash from the escrow on January  
23 5, 1995. There are no other facts or circumstances that would indicate whether, on  
24 September 22, 1994, B had a bona fide intent to enter into a deferred like-kind  
25 exchange.

26  
27 (ii) Under section 1001, B realizes gain to the extent of the amount realized (\$ 100,000)  
28 over the adjusted basis of real property X (\$ 60,000), or \$ 40,000. The terms of the  
29 exchange agreement with D, the identification of properties J, K, and L, the efforts to  
30 have those properties rezoned for commercial purposes, and the absence of other  
31 relevant facts, indicate that B had a bona fide intent at the beginning of the exchange  
32 period to enter into a deferred exchange. Moreover, the limitations imposed in the  
33 exchange agreement on acceptable replacement property do not make it unreasonable  
34 to believe that like-kind replacement property would be acquired before the end of the  
35 exchange period. Therefore, paragraph (j)(2)(iv) of this section does not make  
36 paragraph (j)(2)(i) of this section inapplicable even though B fails to acquire  
37 replacement property. Thus, for purposes of section 453 and § 15a.453-1(b)(3)(i) of  
38 this chapter, the qualified escrow account is disregarded in determining whether B is  
39 in receipt of payment. Accordingly, B is not treated as having received payment on  
40 September 22, 1994, on D's deposit of the \$ 100,000 cash into the qualified escrow  
41 account. Instead, B is treated as receiving payment on January 5, 1995. Subject to the  
42 other requirements of sections 453 and 453A, B may report the \$ 40,000 gain in 1995  
43 under the installment method.

44  
45 (vii) Effective date. This paragraph (j)(2) is effective for transfers of property occurring  
46 on or after April 20, 1994. Taxpayers may apply this paragraph (j)(2) to transfers of  
47 property occurring before April 20, 1994, but on or after June 10, 1991, if those



# EXETER

1031 Exchange Services LLC

1 transfers otherwise meet the requirements of § 1.1031(k)-1. In addition, taxpayers may  
2 apply this paragraph (j)(2) to transfers of property occurring before June 10, 1991, but  
3 on or after May 16, 1990, if those transfers otherwise meet the requirements of §  
4 1.1031(k)-1 or follow the guidance of IA-237-84 published in 1990-1, C.B. See §  
5 601.601(d)(2)(ii)(b) of this chapter.

6  
7 (3) Examples.

8  
9 This paragraph (j) may be illustrated by the following examples.

10  
11 Unless otherwise provided in an example, the following facts are assumed: B, a  
12 calendar year taxpayer, and C agree to enter into a deferred exchange. Pursuant to  
13 their agreement, B is to transfer real property X to C on May 17, 1991. Real property  
14 X, which has been held by B for investment, is unencumbered and has a fair market  
15 value on May 17, 1991, of \$ 100,000. B's adjusted basis in real property X is \$  
16 40,000. On or before July 1, 1991 (the end of the identification period), B is to identify  
17 replacement property that is of a like kind to real property X. On or before November  
18 13, 1991 (the end of the exchange period), C is required to purchase the property  
19 identified by B and to transfer that property to B. To the extent the fair market value  
20 of the replacement property transferred to B is greater or less than the fair market  
21 value of real property X, either B or C, as applicable, will make up the difference by  
22 paying cash to the other party after the date the replacement property is received. The  
23 replacement property is identified as provided in paragraph (c) of this section and is of  
24 a like kind to real property X (determined without regard to section 1031(a)(3) and this  
25 section). B intends to hold any replacement property received for investment.

26  
27 Example 1. (i) On May 17, 1991, B transfers real property X to C and identifies real  
28 property R as replacement property. On June 3, 1991, C transfers \$ 10,000 to B. On  
29 September 4, 1991, C purchases real property R for \$ 90,000 and transfers real  
30 property R to B.

31  
32 (ii) The \$ 10,000 received by B is "money or other property" for purposes of section  
33 1031 and the regulations thereunder. Under section 1031(b), B recognizes gain in the  
34 amount of \$ 10,000. Under section 1031(d), B's basis in real property R is \$ 40,000  
35 (i.e., B's basis in real property X (\$ 40,000), decreased in the amount of money  
36 received (\$ 10,000), and increased in the amount of gain recognized (\$ 10,000) in the  
37 deferred exchange).

38  
39 Example 2. (i) On May 17, 1991, B transfers real property X to C and identifies real  
40 property S as replacement property, and C transfers \$ 10,000 to B. On September 4,  
41 1991, C purchases real property S for \$ 100,000 and transfers real property S to B.  
42 On the same day, B transfers \$ 10,000 to C.

43  
44 (ii) The \$ 10,000 received by B is "money or other property" for purposes of section  
45 1031 and the regulations thereunder. Under section 1031(b), B recognizes gain in the  
46 amount of \$ 10,000. Under section 1031(d), B's basis in real property S is \$ 50,000  
47 (i.e., B's basis in real property X (\$ 40,000), decreased in the amount of money



# EXETER

1031 Exchange Services LLC

1 received (\$ 10,000), increased in the amount of gain recognized (\$ 10,000), and  
2 increased in the amount of the additional consideration paid by B (\$ 10,000) in the  
3 deferred exchange).

4  
5 Example 3. (i) Under the exchange agreement, B has the right at all times to demand \$  
6 100,000 in cash in lieu of replacement property. On May 17, 1991, B transfers real  
7 property X to C and identifies real property T as replacement property. On September  
8 4, 1991, C purchases real property T for \$ 100,000 and transfers real property T to B.

9  
10 (ii) Because B has the right on May 17, 1991, to demand \$ 100,000 in cash in lieu of  
11 replacement property, B is in constructive receipt of the \$ 100,000 on that date. Thus,  
12 the transaction is a sale and not an exchange, and the \$ 60,000 gain realized by B in  
13 the transaction (i.e., \$ 100,000 amount realized less \$ 40,000 adjusted basis) is  
14 recognized. Under section 1031(d), B's basis in real property T is \$ 100,000.

15  
16 Example 4. (i) Under the exchange agreement, B has the right at all times to demand  
17 up to \$ 30,000 in cash and the balance in replacement property instead of receiving  
18 replacement property in the amount of \$ 100,000. On May 17, 1991, B transfers real  
19 property X to C and identifies real property U as replacement property. On September  
20 4, 1991, C purchases real property U for \$ 100,000 and transfers real property U to B.

21  
22 (ii) The transaction qualifies as a deferred exchange under section 1031 and this  
23 section. However, because B had the right on May 17, 1991, to demand up to \$  
24 30,000 in cash, B is in constructive receipt of \$ 30,000 on that date. Under section  
25 1031(b), B recognizes gain in the amount of \$ 30,000. Under section 1031(d), B's basis  
26 in real property U is \$ 70,000 (i.e., B's basis in real property X (\$ 40,000), decreased in  
27 the amount of money that B received (\$ 30,000), increased in the amount of gain  
28 recognized (\$ 30,000), and increased in the amount of additional consideration paid by  
29 B (\$ 30,000) in the deferred exchange).

30  
31 Example 5. (i) Assume real property X is encumbered by a mortgage of \$ 30,000. On  
32 May 17, 1991, B transfers real property X to C and identifies real property V as  
33 replacement property, and C assumes the \$ 30,000 mortgage on real property X. Real  
34 property V is encumbered by a \$ 20,000 mortgage. On July 5, 1991, C purchases real  
35 property V for \$ 90,000 by paying \$ 70,000 and assuming the mortgage and transfers  
36 real property V to B with B assuming the mortgage.

37  
38 (ii) The consideration received by B in the form of the liability assumed by C (\$ 30,000)  
39 is offset by the consideration given by B in the form of the liability assumed by B (\$  
40 20,000). The excess of the liability assumed by C over the liability assumed by B, \$  
41 10,000, is treated as "money or other property." See § 1.1031(b)-1(c). Thus, B  
42 recognizes gain under section 1031(b) in the amount of \$ 10,000. Under section  
43 1031(d), B's basis in real property V is \$ 40,000 (i.e., B's basis in real property X (\$  
44 40,000), decreased in the amount of money that B is treated as receiving in the form of  
45 the liability assumed by C (\$ 30,000), increased in the amount of money that B is  
46 treated as paying in the form of the liability assumed by B (\$ 20,000), and increased in  
47 the amount of the gain recognized (\$ 10,000) in the deferred exchange).





# EXETER

1031 Exchange Services LLC

- 1  
2 (k) Definition of disqualified person.  
3  
4 (1) For purposes of this section, a disqualified person is a person described in  
5 paragraph (k)(2), (k)(3), or (k)(4) of this section.  
6  
7 (2) The person is the agent of the taxpayer at the time of the transaction. For this  
8 purpose, a person who has acted as the taxpayer's employee, attorney, accountant,  
9 investment banker or broker, or real estate agent or broker within the 2-year period  
10 ending on the date of the transfer of the first of the relinquished properties is treated  
11 as an agent of the taxpayer at the time of the transaction. Solely for purposes of this  
12 paragraph (k)(2), performance of the following services will not be taken into account --  
13  
14 (i) Services for the taxpayer with respect to exchanges of property intended to qualify  
15 for nonrecognition of gain or loss under section 1031; and  
16  
17 (ii) Routine financial, title insurance, escrow, or trust services for the taxpayer by a  
18 financial institution, title insurance company, or escrow company.  
19  
20 (3) The person and the taxpayer bear a relationship described in either section 267(b)  
21 or section 707(b) (determined by substituting in each section "10 percent" for "50  
22 percent" each place it appears).  
23  
24 (4)(i) Except as provided in paragraph (k)(4)(ii) of this section, the person and a person  
25 described in paragraph (k)(2) of this section bear a relationship described in either  
26 section 267(b) or 707(b) (determined by substituting in each section "10 percent" for  
27 "50 percent" each place it appears).  
28  
29 (ii) In the case of a transfer of relinquished property made by a taxpayer on or after  
30 January 17, 2001, paragraph (k)(4)(i) of this section does not apply to a bank (as  
31 defined in section 581) or a bank affiliate if, but for this paragraph (k)(4)(ii), the bank  
32 or bank affiliate would be a disqualified person under paragraph (k)(4)(i) of this section  
33 solely because it is a member of the same controlled group (as determined under  
34 section 267(f)(1), substituting "10 percent" for "50 percent" where it appears) as a  
35 person that has provided investment banking or brokerage services to the taxpayer  
36 within the 2-year period described in paragraph (k)(2) of this section. For purposes of  
37 this paragraph (k)(4)(ii), a bank affiliate is a corporation whose principal activity is  
38 rendering services to facilitate exchanges of property intended to qualify for  
39 nonrecognition of gain under section 1031 and all of whose stock is owned by either a  
40 bank or a bank holding company (within the meaning of section 2(a) of the Bank  
41 Holding Company Act of 1956 (12 U.S.C. 1841(a)).  
42  
43 (5) This paragraph (k) may be illustrated by the following examples. Unless otherwise  
44 provided, the following facts are assumed: On May 1, 1991, B enters into an exchange  
45 agreement (as defined in paragraph (g)(4)(iii)(B) of this section) with C whereby B  
46 retains C to facilitate an exchange with respect to real property X. On May 17, 1991,  
47 pursuant to the agreement, B executes and delivers to C a deed conveying real





# EXETER

1031 Exchange Services LLC

1 property X to C. C has no relationship to B described in paragraphs (k)(2), (k)(3), or  
2 (k)(4) of this section.  
3

4 Example 1. (i) C is B's accountant and has rendered accounting services to B within  
5 the 2-year period ending on May 17, 1991, other than with respect to exchanges of  
6 property intended to qualify for nonrecognition of gain or loss under section 1031.  
7

8 (ii) C is a disqualified person because C has acted as B's accountant within the 2-year  
9 period ending on May 17, 1991.  
10

11 (iii) If C had not acted as B's accountant within the 2-year period ending on May 17,  
12 1991, or if C had acted as B's accountant within that period only with respect to  
13 exchanges intended to qualify for nonrecognition of gain or loss under section 1031, C  
14 would not have been a disqualified person.  
15

16 Example 2. (i) C, which is engaged in the trade or business of acting as an  
17 intermediary to facilitate deferred exchanges, is a wholly owned subsidiary of an  
18 escrow company that has performed routine escrow services for B in the past. C has  
19 previously been retained by B to act as an intermediary in prior section 1031  
20 exchanges.  
21

22 (ii) C is not a disqualified person notwithstanding the intermediary services previously  
23 provided by C to B (see paragraph (k)(2)(i) of this section) and notwithstanding the  
24 combination of C's relationship to the escrow company and the escrow services  
25 previously provided by the escrow company to B (see paragraph (k)(2)(ii) of this  
26 section).  
27

28 Example 3. (i) C is a corporation that is only engaged in the trade or business of acting  
29 as an intermediary to facilitate deferred exchanges. Each of 10 law firms owns 10  
30 percent of the outstanding stock of C. One of the 10 law firms that owns 10 percent of  
31 C is M. J is the managing partner of M and is the president of C. J, in his capacity as  
32 a partner in M, has also rendered legal advice to B within the 2-year period ending on  
33 May 17, 1991, on matters other than exchanges intended to qualify for nonrecognition  
34 of gain or loss under section 1031.  
35

36 (ii) J and M are disqualified persons. C, however, is not a disqualified person because  
37 neither J nor M own, directly or indirectly, more than 10 percent of the stock of C.  
38 Similarly, J's participation in the management of C does not make C a disqualified  
39 person.  
40

41 (1) [Reserved]  
42

43 (m) Definition of fair market value.  
44

45 For purposes of this section, the fair market value of property means the fair market  
46 value of the property without regard to any liabilities secured by the property.  
47



# EXETER

*1031 Exchange Services LLC*

1 (n) No inference with respect to actual or constructive receipt rules outside of section  
2 1031.

3  
4 The rules provided in this section relating to actual or constructive receipt are  
5 intended to be rules for determining whether there is actual or constructive receipt in  
6 the case of a deferred exchange. No inference is intended regarding the application of  
7 these rules for purposes of determining whether actual or constructive receipt exists  
8 for any other purpose.

9  
10 (o) Effective date.

11  
12 This section applies to transfers of property made by a taxpayer on or after June 10,  
13 1991. However, a transfer of property made by a taxpayer on or after May 16, 1990,  
14 but before June 10, 1991, will be treated as complying with section 1031 (a)(3) and  
15 this section if the deferred exchange satisfies either the provision of this section or the  
16 provisions of the notice of proposed rulemaking published in the FEDERAL REGISTER  
17 on May 16, 1990 (55 FR 20278).