



## Impact of Section 1031 Modification to Rollover Structure

### Internal Revenue Code Section 1031

Since 1921, Federal tax law under IRC section 1031 has permitted a taxpayer to exchange business-use or investment assets for other like-kind business use or investment assets without recognizing taxable gain on the sale of the old assets. The taxes, which otherwise would have been due from the sale, are thus deferred. These can range from relatively simple transactions involving commercial, agricultural and rental real estate to more complex transactions involving aircraft, trucks, trailers, containers, railcars, agricultural equipment, other heavy equipment, livestock and other assets. Most 1031 Exchanges involve separate buyers and sellers and are not simple swaps between two parties. Under these circumstances, tax rules require the use of an independent third party Qualified Intermediary (QI). The QI holds the sale proceeds for the benefit of the taxpayer during the exchange, disbursing funds for purchase of like-kind replacement property, and returning any unused funds to the taxpayer at the end of the exchange. Section 1031 Exchanges must be completed within 180 days. Taxpayers recognize gain and pay tax on any unused funds or when they ultimately “cash out” of their property.

### Tax Simplification “Rollover” Proposal

Proposals have been made from time to time to “simplify” IRC section 1031 by shifting to a “rollover” structure. This **would not simplify 1031 Exchange** practice, but rather would result in **more complexity** for taxpayers, eliminate the value provided by the QI, and reduce the compliance rate for 1031 Exchange transactions. QIs create and provide necessary documentation for 1031 Exchanges, serve as a resource to taxpayers and their advisors, and as unofficial compliance officers for the IRS. **The Federation of Exchange Accommodators (“FEA”) strongly opposes conversion of section 1031 to a “rollover” because it is unneeded, less user-friendly and more costly to taxpayers.** Ultimately such a proposal would put QIs out of business, harming predominantly small businesses that provide customers with a useful service at a reasonable price.

- **A rollover would be problematic from an enforcement standpoint, would create uncertainty in the process, and would open the floodgates for both unintentional as well as intentional abuse, resulting in a revenue negative impact upon the US Treasury.**
- **Professional Qualified Intermediaries provide technical services beyond the mere holding of taxpayers’ exchange funds.** QIs actually make the process simpler because they guide taxpayers and their advisors through the exchange process.
- **FEA member QIs are subject matter experts in the realm of 1031 Exchanges,** providing information, education and training to taxpayers and their accountants, attorneys, financial advisors and real estate brokers. Many FEA members have attorneys, accountants and industry-credentialed Certified Exchange Specialists® on staff.



# 1031 Tax Reform Updates

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- » **QIs routinely inform taxpayers and their advisors of the rules related to Like-Kind Exchanges**, including whether proposed transactions will meet the standards to qualify for exchange treatment, and whether particular properties are like-kind.
- » **QIs typically are paid a modest fee** to facilitate a specific exchange and **do not usually receive any additional fees for all of the educational and resource services provided** to the advisor community and to taxpayers.
- » **Without QIs, taxpayers' costs for engaging in a 1031 Exchange would increase significantly** because they would have to pay attorneys and accountants at professional services rates to receive exchange documentation and information about 1031 Exchange requirements. Professional QIs provide an efficient package of exchange facilitation services; thus QI fees tend to be commoditized and relatively low compared to advisory fees for information and documentation not rising to the level of professional advice.
- » **The QI safe harbor provides a substantial free benefit to the government because QIs promote compliance with the technical requirements for proper exchange treatment, without which, tax revenue would decrease through improperly claimed section 1031 treatment and increased auditing costs.** QIs frequently receive questions from potential clients about exchanges involving non-qualifying property or other breaches of the tax rules. Some QIs estimate that as many as 50% of the inquiries they receive are based upon transactional factors that do not properly qualify for section 1031 treatment. QIs promote compliance by declining to facilitate exchanges that clearly are outside of the rules, and by educating the uninformed about what those rules are.