

Qualified “Like-Kind” Property

There is a two-pronged test for properties to qualify for IRC §1031 tax-deferral treatment.

1. Both the Relinquished and the Replacement Properties must be held by the Exchanger either for investment purposes or for productive use in a trade or business. The Exchanger’s purpose and intent in holding the property is the critical test. The use of the property by other parties to the exchange (Relinquished Property buyer or Replacement Property seller) is irrelevant.
2. The Relinquished and the Replacement Properties must also be “like-kind.” The term “like-kind” refers to the nature or character of the property, ignoring differences of grade or quality. For example, unimproved real property is considered like-kind to improved real property, because the lack of improvements is a distinction of grade or quality; the basic real estate nature of both parcels is the same. Treas. Reg. §1.1031(a)-1(b). In essence, all real property in the United States is “like-kind” to all other domestic real property. However, for personal property assets the definitions are narrower. Exchanged personal property assets must be either like-kind (i.e. an airplane for an airplane or a painting for a painting) or “like-class.” The “like-class” distinction applies to tangible, depreciable business use assets that are included within the same General Asset Class or Product Class, permitting an exchange of an airplane for a helicopter, or a road grader for a back hoe or other item of construction machinery and equipment.

Following are examples of qualifying properties that could be exchanged:

- Raw land or farmland for improved real estate
- Oil & gas royalties for a ranch
- Fee simple interest in real estate for a 30-year leasehold or a Tenant-in-Common interest in real estate
- Residential, Commercial, Industrial or Retail rental properties for any other real estate
- Rental ski condo for a three-unit apartment building
- Corporate jet for an airplane or a helicopter
- Buses for buses
- Dairy cows for dairy cows; Race horse for a race horse (Note: livestock of different sexes are not like-kind)
- Bulldozer for backhoe or other construction machinery and equipment
- Mitigation credits for restoring wetlands for other mitigation credits
- Beer distribution routes for beer distribution routes
- Software patent for another software patent
- Painting for a painting; sculpture for a sculpture

Under IRC §1031, the following properties do not qualify for tax-deferred exchange treatment:

- Stock in trade or other property held primarily for sale (i.e. property held by a developer, “flipper” or other dealer)
- Securities or other evidences of indebtedness or interest
- Stocks, bonds, or notes
- Certificates of trust or beneficial interests
- Interests in a partnership
- Choses in action (rights to receive money or other property by judicial proceeding)
- Foreign property (real or personal) for U.S. based property
- Goodwill of one business for goodwill of another business