Do You Want 360 Days to Exchange?

Combine a Reverse Exchange Followed by a Delayed Exchange

1031
Knowledge

SAFE HARBOR GUIDANCE

Tax-deferred exchanges have been part of the U.S. Tax Code since 1921. Since that time, the government has approved certain methods to structure exchange transactions that are so-called “safe harbors.” For example, in 1991 the U.S. Treasury issued final regulations that provided important guidance on the structure of delayed exchanges including the 45-day identification period and 180-day exchange period timelines and certain other procedural requirements necessary to complete a tax-deferred exchange safely. On September 15, 2000, the Internal Revenue Service released Revenue Procedure 2000-37 that provided guidelines for structuring reverse exchanges (a transaction in which replacement property is acquired by an accommodating party before the sale of the relinquished property and held as replacement property to complete the exchange). A replacement property may be acquired and held (sometimes called “parked”) by the accommodating party for up to 180 calendar days. The IRS provided guidance (*See* ILM 200836024) approving the combination of a reverse parking arrangement exchange and a forward delayed exchange resulting in two sequential 180-day exchange periods associated with one exchange transaction.

Since the accommodating party in a reverse exchange can only hold the replacement property for 180 days, the relinquished property must generally be sold by the taxpayer within that 180-day accommodation period. If the parked replacement property is the only property that is desired by the taxpayer to complete the exchange, then the exchange is complete upon the accommodator’s transfer of the replacement property to the exchanger. But what if the parked replacement property is just one of several replacement properties desired by the taxpayer? In that event, the standard delayed exchange that commences with the sale of the relinquished property may be used to acquire other replacement properties over the second 180-day exchange period commencing with the sale of the relinquished property. In this fashion, the exchange transaction spans two exchange periods starting with the accommodator’s acquisition of the parked property and ending on the exchanger’s acquisition of the last replacement property, potentially spanning 360 calendar days.

Suppose that an exchanger owns an office building in Parsippany, NJ which he has contracted to sell for $10,000,000 to close in December 2020. The exchanger would like to take advantage of a couple of excellent opportunities to purchase property in the Northeast at a significant discount. The investor negotiates to purchase one such property in Westchester, NY for $4,000,000. The investor acquires such property by using a reverse exchange which closes at the end of August 2020. When the relinquished property in Parsippany is finally sold in December 2020 as part of a regular delayed exchange, the net sale proceeds are used to purchase the parked Westchester replacement property held by the accommodator. Now, in this second leg of the exchange transaction, the exchanger has 45 days following the sale of the relinquished property in Parsippany to identify other suitable replacement property to spend the remaining $6,000,000 needed to obtain 100% deferral and a maximum of 180 days to close on one or more identified replacement properties.

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