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Structuring Like-Kind Real Estate Exchange Treatment

September 30, 2020

It is a commonly held belief among real estate investors that they will be entitled to like-kind exchange treatment under the Internal Revenue Code (the "Code") if they sell real property (commonly referred to as a "relinquished property") and use the cash proceeds to acquire another real property (commonly referred to as an "exchange property") as long as they (i) identify the exchange property no more than 45-days after the relinquished property is transferred; and (ii) acquire the exchange property no more than 180-days after that transfer occurs. While sometimes true, this could be a trap for the unwary when a calendar year taxpayer sells real property after October 17 (October 18 if the following year is a leap year) of any year.

The Code requires that a seller seeking like-kind exchange treatment acquire the exchange property within the period beginning on the day on which he transferred title to the relinquished property and ending ***on the earlier of*** the 180th day thereafter or the due date (determined with regard to extensions) for his federal income tax return. Consequently, a calendar year seller who does not file a timely request for an automatic six-month extension for the year in which he sells relinquished property will have fewer than 180 days within which to acquire an exchange property if the sale of the relinquished property occurs after October 17 (October 18 if the following year is a leap year). On the other hand, a calendar year taxpayer who files a timely request for an automatic six-month extension for the year in which he sells relinquished property will, in all cases, have 180 days within which to acquire an exchange property.

Real estate investors should keep the calendar in mind when structuring a like-kind real estate exchange to make certain they can avail themselves of the beneficial tax treatment afforded by Section 1031 of the Code.

The Secretary of the Treasury has the authority to postpone the due date for filing federal income tax returns for taxpayers affected by, among other things, a federally declared disaster. Any such postponement most likely would eliminate the trap discussed above. While the Secretary has issued what he refers to as a "Covid-19 Postponement" in which he postponed until July 15, 2020 the due date for filing Forms 1040 otherwise due (originally or pursuant to a valid extension) on or after April 1, 2020, there is no basis for assuming he will take similar action with respect to filing Forms 1040 due in 2021.

If you are engaged in a like-kind exchange of real property or would like assistance structuring one, please contact Barry Klingman.

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