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Insights

Section 1031 Exchanges: Final Regulations Issued for Definition of Real Property

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Under Internal Revenue Code, Section 1031 ("Section 1031"), the taxpayer may exchange certain property for other like property and defer gain recognition on the relinquished property. The Tax Cuts and Jobs Act of 2017 ("TCJA") limited the application of Section 1031 to only exchanges of real property that is held for use in a trade or business or for investment (not held primarily for sale). Under TCJA, exchanges of personal or non-real estate intangible property such as machinery, equipment, vehicles, art work, collectibles, patents and other intellectual property will not qualify for the tax-free treatment under Section 1031.

There was some consternation that TCJA did not define real property but left us to the subsequent determination by the Internal Revenue Service ("IRS"). The IRS has now issued Final Regulations, TD 9935, effective December 2, 2020 defining real property. As hoped, the Final Regulations provide that property defined as real property under state law is real property for purposes of Section 1031. Examples of real property are land and improvements to land, unsevered natural products of land, and water and air space adjacent to land. Intangibles that may be treated as real property, in addition to fee simple ownership, are leasehold interests, options to purchase, easements, interests in cooperative housing corporations and shares in real estate assets that are treated as real estate under state law. Incidental personal property may be included in limited instances.

The Krieg DeVault **Real Estate & Environmental Practice** follows the availability of Section 1031 for real estate transactions. If you have any further questions or concerns about the content of this Alert, or any other real estate issues, please contact **Christopher D. Long** or a member of Krieg DeVault's **Real Estate & Environmental Practice**.

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