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Person To Contact:
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Telephone Number:

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PLR-132683-12
Date:
November 15, 2012

TY:

LEGEND:

Applicant =
Parent =

Dear

This responds to your request for a private letter ruling, dated July 26, 2012, concerning how the software you provide to like-kind exchange program (LKE Program) clients affects your status as a qualified intermediary (QI) under § 1.1031(k)-1(g)(4) of the Income Tax Regulations.

FACTS

Parent is a tax and business advisory firm. Parent owns 90 percent of Applicant, an affiliate company that provides services to its clients relating to exchanges of property under § 1031 of the Internal Revenue Code. Applicant and Parent are both partnerships for tax purposes using an annual accounting period ending December 31, and the cash method of accounting for maintaining their books and records and filing their federal income tax returns.

Applicant provides § 1031 services to two types of exchange clients: (1) clients that engage in single exchange transactions (*e.g.,* an exchange of investment real estate), and (2) clients that engage in series of ongoing exchanges of tangible personal property (referred to as LKE Programs). Applicant serves as the QI for both types of clients. Applicant is not related to any of its clients in the manner described in either § 267(b) or § 707(b).

Applicant provides its LKE clients with its in-house developed software. The software allows clients to track and manage their exchanges and helps Applicant fulfill its obligations as QI. Specifically, a client using the software can (i) match relinquished and replacement properties, (ii) prepare and submit 45-day identifications, and (iii) compute depreciation and gain or loss on the LKE Program assets. The Applicant uses this software to enforce the restrictions on the use of the exchange funds under § 1.1031(k)-1(g)(6) of the regulations and to ensure proper identification of replacement property. This software is not otherwise commercially available.

Applicant provides no services to its clients other than services relating to like-kind exchanges of property. Neither Parent nor any other party related to Applicant provides any other services to Applicant's clients. Applicant and Parent do not prepare or sign the tax returns of Applicant's clients. Applicant and Parent have a firm policy against providing other services to Applicant's clients. Furthermore, Applicant only receives a fee from its clients for services relating to the exchanges of property. In no event has Applicant ever replaced a client's accountant or tax advisor, or assumed any of the duties or responsibilities of the client's regular accountant or advisor.

LAW AND ANALYSIS

Section 1031(a)(1) of the Code provides that no gain or loss is recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind to be held either for productive use in a trade or business or for investment.

Section 1031(a)(3) limits the time for the identification and receipt of replacement property for non-simultaneous (or deferred) like-kind exchanges. It provides that any property received by the taxpayer is treated as non like-kind property if-- (A) such property is not identified as property to be received in the exchange within 45 days of the date on which the taxpayer transfers the property relinquished in the exchange, or (B) such property is received after the earlier of-- (i) 180 days after the date on which the taxpayer transfers the property relinquished in the exchange, or (ii) the due date (determined with regard to extension) for the transferor's tax return for the taxable year in which the transfer of the relinquished property occurs.

In addition to the timing limitations for identification and replacement, § 1031(b) provides that gain realized in an exchange is recognized to the extent of the money or fair market value of other non-like-kind property (boot) received by an exchanging taxpayer in the exchange. Section 1.1031(k)-1(f)(1) of the regulations provides that gain or loss may be recognized if the taxpayer actually or constructively receives money or other property before the taxpayer actually receives like-kind replacement property. If the taxpayer actually or constructively receives money or other property in the full amount of the consideration for the relinquished property before the taxpayer receives like-kind replacement property, the transaction will constitute a sale and not a deferred

exchange, even though the taxpayer may ultimately receive like-kind replacement property.

The Income Tax Regulations under § 1031 also provide various safe harbors by which a taxpayer may avoid having actual or constructive receipt of boot in a deferred exchange. One safe harbor involves the use of a qualified intermediary. Section 1.1031(k)-1(g)(4)(i) provides that in the case of a taxpayer's transfer of relinquished property involving a qualified intermediary, the qualified intermediary is not considered the agent of the taxpayer for purposes of § 1031(a). In such a case, the taxpayer's transfer of relinquished property and subsequent receipt of like-kind replacement property is treated as an exchange, and the determination of whether the taxpayer is in actual or constructive receipt of money or other property before the taxpayer actually receives like-kind replacement property is made as if the qualified intermediary is not the agent of the taxpayer.

Section 1.1031(k)-1(g)(4)(ii) provides that the qualified intermediary safe harbor applies only if the agreement between the taxpayer and the qualified intermediary expressly limits the taxpayer's rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held by the qualified intermediary as provided in § 1.1031(k)-1(g)(6).

Section 1.1031(k)-1(g)(4)(iii) defines a qualified intermediary as a person who-- (A) is not the taxpayer or a disqualified person, and (B) enters into a written agreement with the taxpayer (the "exchange agreement") and, as required by the exchange agreement, acquires the relinquished property from the taxpayer, transfers the relinquished property, acquires the replacement property, and transfers the replacement property to the taxpayer.

Section 1.1031(k)-1(k)(2) defines a "disqualified person" to include an agent of the taxpayer at the time of the transaction. For this purpose, a person who has acted as the taxpayer's employee, attorney, accountant, investment banker or broker, or real estate agent or broker within the 2–year period ending on the date of the transfer of the first of the relinquished properties is treated as an agent of the taxpayer at the time of the transaction. Performance of the following services is not taken into account in determining whether a person is a disqualified person-- (i) services for the taxpayer with respect to exchanges of property intended to qualify for nonrecognition of gain or loss under § 1031; and (ii) routine financial, title insurance, escrow, or trust services for the taxpayer by a financial institution, title insurance company, or escrow company. In addition, § 1.1031(k)-1(k)(4)(i) generally provides that a person who bears a relationship (as described in either § 267(b) or § 707(b), determined by substituting in each section "10 percent" for "50 percent" each place it appears) with a person described in § 1.1031(k)-1(k)(2) is a disqualified person.

In this case, Applicant's providing of its software to its LKE program clients does not make Applicant an agent of its clients. The software supplied by Applicant enables an LKE program client to manage a high volume of exchange transactions. The software also assists Applicant in fulfilling its obligations as QI. The matching of relinquished and replacement properties and preparing and submitting 45-day identifications are services described in § 1.1031(k)-1(k)(2)(i) and thus not taken into account in determining whether Applicant is an agent. In addition, although the software also computes depreciation and the gain or loss from an LKE Program client's transactions, these functions do not result in Applicant being considered an accountant for its clients. The depreciation and gain or loss functions are essentially automated math calculations based on data input by the LKE Program client and do not rise to the level of an accountant/client or other agency relationship. Accordingly, Applicant is not a disqualified person to an LKE Program client under § 1.1031(k)-1(k) as a result of providing software with the functions described.

RULING

Applicant is not a disqualified person, as defined in § 1.1031(k)-1(k), for providing the described software to its LKE Program clients.

DISCLAIMERS

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations submitted by Applicant and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Michael J. Montemurro
Chief, Branch 4
(Income Tax & Accounting)

cc: