

# CHICAGO DEFERRED EXCHANGE COMPANY

## RELATED PARTIES

### Revenue Ruling 2002-83

As part of the Revenue Reconciliation Act of 1989, Section 1031(f)(1) added a required two-year holding period on exchanges between related parties.

The language of the statute at §1031(f)(2) contains specific exceptions to the two-year holding period, including transfers within the two years as a result of involuntary conversion or death of the Taxpayer or a related party. Additionally, in situations where the Taxpayer can establish, to the satisfaction of the IRS, that neither the exchange nor the subsequent disposition within the two-year period had, as one of its principal purposes, the avoidance of federal income tax, a disposition before the end of the two-year period will not disqualify the exchange.

There had been much uncertainty on the appropriate application of §1031(f) to exchanges between related parties where a Taxpayer acquires property from a related party due in part to several PLRs, TAMs, and FSAs issued by the IRS in the last several years.

In November of 2002, the IRS published Revenue Ruling 2002-83 in an attempt to clarify its position on the application of §1031(f)(4) — which provides that the nonrecognition rules of Section 1031 do not apply to any transaction (or series of transactions) structured to avoid the purposes of the related party rules.

The Revenue Ruling addresses the following scenario:

1. Taxpayer sells relinquished property with FMV of \$150 and basis of \$50 to an unrelated third party purchaser.
2. Taxpayer transfers the relinquished property, through a Qualified Intermediary, directly to an unrelated third party purchaser.
3. Taxpayer acquires replacement property with a FMV of \$150 from a related party. The property's basis in the related party's hands is \$150.
4. Related party transfers replacement property, through a Qualified Intermediary, directly to Taxpayer.

The Revenue Ruling concludes that Taxpayer is using the Qualified Intermediary to "circumvent the purposes" of §1031(f) and that, as provided in §1031(f)(4), the non-recognition provisions afforded by §1031 will not apply.

The conclusion of the Revenue Ruling is consistent with TAM 9748006. It appears from the example in the Revenue Ruling, and the facts of the TAM, that Taxpayer never intended to acquire any property other than the related party property.

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