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- When can you make an offer on a Replacment Property Contract
- Partnership Exchanges

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When Can You Make an Offer on a Replacement Property? You can write a contract making an offer to purchase the replacement property at any time. You may use your own funds to make an earnest money deposit. Exchangors sometimes confuse the ironclad restriction that you may not go to settlement on the replacement property until you go to settlement on the relinquished property with making a contract offer. There is no restriction on when you may make a contract offer on the replacement property. Despite rumors to the contrary IRC 1031 has not been changed to permit a reverse exchange. A taxpayer still may not close on a new replacement property before closing and transferring the old relinquished property.

What did happen was that "Revenue Procedure 2000-37: Procedures for Accommodation of Reverse Exchanges" was published establishing "safe harbor" rules permitting a third party "exchange accommodation titleholder (EAT)" to take legal title to the desired replacement property.
The EAT, a special purpose business entity, will then own and operate the replacement property until the taxpayer is able to close on the relinquished property. The exchangor, using a Qualified Intermediary, can then close in the proper sequence on the relinquished and replacement properties. The Fall 2000 Real Estate Exchange News on our Web site has a complete explanation of the rules set forth in Revenue Procedure 2000-37.

Partnerships and a Like Kind Exchange. Many taxpayers own an interest in a partnership that owns business, rental or investment real estate. Internal Revenue Code Section 1031(a)(2)(D) is very clear when it states "interest in a partnership may not be exchanged". There is no question that a partnership may as an entity do its own exchange. The problem occurs when the taxpayer owns an interest in a partnership and the other partner(s) wish to go their own way. They wish to exchange for a different property or just sell and pay the capital gains tax.

There are three basic partnership situations that we encounter. **First**, is the situation where the title to the property is in the name of the partnership and the partnership files an annual partnership tax return. It is clear that the individual partners own an interest in the partnership and not in the real estate, and thus cannot exchange their interest for another property. A common solution is for the partnership to be dissolved, distributing the property to the partners as tenants-in-common. Each co-owner can then exchange their interest in the property for a separate replacement property or pay the tax. An alternative is for the partnership to do an exchange for a number of replacement properties. Then the partnership is dissolved, distributing the desired replacement property to each partner.

The **second** situation is where the title to the property is held by the individual taxpayers, but they may have a partnership agreement and file partnership returns. In this case the parties may elect under IRC Section 761(a) to not be treated as a partnership. Then each co-owner will be treated as owning an undivided interest in the real estate and may complete a like kind exchange under Section 1031.

> Action. If your partnership plans on selling its property and you desire to do an exchange you should meet as soon as possible with your tax accountant and partnership attorney to determine what actions must be taken. The solutions to the above two situations are not without tax risk. There are specific actions that need to be taken to insure a successful like kind exchange. Professional legal and tax advise is essential. Advisors are encouraged to refer to Chapter 9, Tax-Free Exchanges Under Section 1031, by Jeremiah Long and Mary Foster, and published by West Group.

The **third** situation is where the title is in the name of the individual co-owners, and each co-owner reports income, expenses and depreciation,etc. on their own tax return. Usually on Schedule E. Even though they may call themselves partners, they are usually treated as individual owners of an undivided interest in the real estate. As such, they may exchange their interest in the relinquished property for a partial or whole interest in one or more replacement properties.