

COMPLIMENTS OF:



580 JENSEN GROVE DRIVE  
PO BOX 339  
BLACKFOOT, ID 83221  
PH: 1.877.782.2515  
FAX: 1.208.785.2575  
WWW.EXCHANGE-SERVICESINC.COM



1006 WEST SUSSEX AVENUE  
PO BOX 549  
MISSOULA, MT 59801  
PH: 1.866.348.2577  
FAX: 1.406.541.4005  
WWW.MTEXCHANGESERVICES.COM

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## Valuable Information for Real Estate Professionals and their Clients

# EASEMENTS AND CONSERVATION EASEMENTS

### WHAT IS A §1031 EXCHANGE?

A §1031 tax deferred exchange is a method by which a taxpayer trades like-kind property, held for investment or business purposes, for like-kind replacement property resulting in deferral of capital gains tax on the transaction.

### WHAT IS CONSIDERED LIKE-KIND PROPERTY?

In general, all property or equipment held for investment purposes or used in a business or trade qualifies for exchange treatment. The term "like-kind" refers to the nature of the property, rather than its grade or quality. Real property must be exchanged for other like-kind real property and is not considered like-kind to personal property.

The like-kind standard for real property is extremely broad. In essence, any real property which is held for *productive use in a trade or business or for investment* is considered like-kind. This property can be improved or unimproved as it will not affect the nature or character of the property.

### DOES AN EASEMENT QUALIFY FOR AN EXCHANGE?

In many transactions, an easement is considered to be like-kind to other like-kind real property held for investment or business purposes. Although, it is imperative to look at the treatment of easements under the applicable state laws. If considered real property, an easement may be able to be exchanged for an apartment building, farm land, or possibly rental resort property. Consult with your tax professional to ensure that the property you want to exchange will qualify for tax deferred treatment.

### EXCHANGE REQUIREMENTS

- ▶ The old (relinquished) property and the new (replacement) property must be like-kind to one another and used for business or investment purposes.
- ▶ The replacement property(ies) must be identified no later than 45 days after the date of closing on your relinquished property. Also, the replacement property(ies) must be acquired no later than 180 days after the date of closing on your relinquished property.
- ▶ If your intent is to defer 100% of the gain, the new property should be equal or greater in value than the property which was sold. In addition, the entire net equity must be reinvested into the new property(ies)
- ▶ The taxpayer must remain consistent throughout the duration of the exchange transaction.
- ▶ The taxpayer may not receive the proceeds from the sale. The most common structure utilizes a "Qualified Intermediary" as an approved middleman.

### QUALIFYING EASEMENT EXCHANGES

- ▶ An agricultural easement for a fee simple interest in real property. *IRS Letter Ruling 9232030*
- ▶ A conservation easement for a fee simple interest in commercial real property. *IRS Letter Ruling 9601046*
- ▶ A scenic conservation easement for a fee simple interest in farm land. *IRS Letter Ruling 9621012*