

1031 NEWS

VACATION HOMES AND IRC § 1031 SAFE HARBOR Internal Revenue Procedure 2008-16 Effective: March 10, 2008

In *Moore v. Commissioner*, T.C. Memo. 2007-134, the taxpayers exchanged one lakeside vacation home for another. Neither home

TAXPAYERS MUST PLAN YEARS AHEAD IN ORDER TO DO A 1031 ON THEIR VACATION HOME!!!



was ever rented. Both were used by the taxpayers only for per-

sonal purposes. The taxpayers claimed that the exchange of the homes was a like-kind exchange under § 1031 because the properties were expected to appreciate in value and thus were held for investment. The Tax Court held, however, that the properties were held for personal use and that the "mere hope or expectation that property may be sold at a gain cannot establish an investment intent if the taxpayer uses the property as a residence."

The Service recognizes that many taxpayers hold dwell-

ing units primarily for the production of current rental income, but also use the properties occasionally for personal purposes. In the interest of sound tax administration, this revenue procedure provides taxpayers with a safe harbor under which a dwelling unit will qualify as property held for productive use in a trade or business or for investment under § 1031 even though a taxpayer occasionally uses the dwelling unit for personal purposes.

Qualifying Use Standards

In general. The Service will not challenge whether a dwelling unit qualifies under § 1031 as property held for productive use in a trade or business or for investment if the following qualifying use standards of are met for the dwelling unit.

(1) Relinquished property.

A dwelling unit that a taxpayer intends to be relinquished property in a § 1031 exchange qualifies as property held for productive use in a trade or business or for investment if:

- (a) The dwelling unit is owned by the taxpayer for at least 24 months immediately before the exchange (the "qualifying use period"); and
- (b) Within the qualifying use period, in each of the two 12-month

periods immediately preceding the exchange,

- (i) The taxpayer rents the dwelling unit to another person or persons at a fair rental for 14 days or more, and
- (ii) The period of the taxpayer's personal use of the dwelling unit does not exceed the greater of 14 days or 10 percent of the number of days during the 12-month period that the dwelling unit is rented at a fair rental.

For this purpose, the first 12-month period immediately preceding the exchange ends on the day before the exchange takes place (and begins 12 months prior to that day) and the second 12-month period ends on the day before the first 12-month period begins (and

begins 12 months prior to that day).

(2) Replacement property. A dwelling unit that a taxpayer intends to be replacement property in a § 1031 exchange qualifies as property held for productive use in a trade or business or for investment if:

- (a) The dwelling unit is owned by the taxpayer for at least 24 months immediately after the exchange (the "qualifying use period"); and
- (b) Within the qualifying use period, in each of the two 12-month periods immediately after the exchange,
 - (i) The taxpayer rents the dwelling unit to another person or persons at a fair rental for 14 days or more, and

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KEY POINTS FOR TAXPAYER TO REMEMBER:

- > Must RENT for 14 days or more per year!
- > Must OWN for 2 years or more!
- > Limit Personal Use:
Can only use 14 days per year or 10% of rental period if greater!

Required for BOTH Relinquished & Replacement Properties!

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Qualifying Use Standards (continued)

(ii) The period of the taxpayer's personal use of the dwelling unit does not exceed the greater of 14 days or 10 percent of the number of days during the 12-month period that the dwelling unit is rented at a fair rental.

For this purpose, the first 12-month period immediately after the exchange begins on the day after the exchange takes place and the second 12-month period begins on the day after the first 12-month period ends.

Personal use. For purposes of this revenue procedure, personal use of a dwelling unit occurs on any day on which a taxpayer is deemed to have used the dwelling unit for personal purposes under § 280A(d)(2) (taking into account § 280A(d)(3) but not § 280A(d)(4)).

Fair rental. For purposes of this revenue procedure, whether a dwelling unit is rented at a fair

rental is determined based on all of the facts and circumstances that exist when the rental agreement is entered into. All rights and obligations of the parties to the rental agreement are taken into account.

Special rule for replacement property. If a taxpayer files a federal income tax return and reports a transaction as an exchange under § 1031, based on the expectation that a dwelling unit will meet the qualifying use standards in section 4.02(2) of this revenue procedure for replacement property, and subsequently determines that the dwelling unit does not meet the qualifying use standards, the taxpayer, if necessary, should file an amended return and not report the transaction as an exchange under § 1031.

Limited application of safe harbor. The safe harbor provided in this revenue procedure applies

only to the determination of whether a dwelling unit qualifies as property held for productive use in a trade or business or for investment under § 1031. A taxpayer utilizing the safe harbor in this revenue procedure also must satisfy all other requirements for a like-kind exchange under § 1031 and the regulations thereunder.

Effective Date: This revenue procedure is effective for exchanges of dwelling units occurring on or after March 10, 2008. No inference is intended with respect to the federal income tax treatment of exchanges of dwelling units occurring prior to the effective date of this revenue procedure.

The principal author of the revenue procedure is J. Peter Baumgarten of the Office of Associate Chief Counsel (Income Tax & Accounting).



MEET THE PRESIDENT CLAIRE WESTBERG

PRESIDENT/OWNER

SPECTRUM EXCHANGE CORP. & ALL REAL PROPERTY, INC.

Claire began her career in California, as an escrow officer specializing in residential resale and commercial transactions. She handled her first exchange in 1979. She launched her 1031 companies in 1995 and has done thousands of exchanges ever since. She specializes in the more complex reverse and build-to-suit transactions and takes pride in educating and guiding her clients every step of the way.

You can contact her anytime with 1031 exchange questions!

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