What is a Like-Kind Exchange: Internal Revenue Code §1031 allows for deferral of capital gains tax and ordinary income tax on business or investment property if the property is exchanged for like-kind business or investment property.

Why Do a Like-Kind Exchange: The Like- Kind Exchange Rules (LKE) encourage investment and reinvestment in U.S. assets. The LKE rules make it easier for taxpayers to relocate or upgrade into assets that better meet their business needs. Like-kind exchanges are used extensively by small businesses in multiple industries, including real estate, transportation, equipment rental and leasing, and construction.

What Types of Assets are Exchanged:

- → Commercial and industrial real estate;
- → Multifamily residential real estate;
- → Agricultural land;
- → Farm machinery and equipment;
- → Breeding and productive livestock (i.e. dairy cows);
- → Construction machinery and equipment;
- → Rental cars and rental equipment;
- → Leased trucks, cars, railcars and equipment;
- → Over the road tractors, trailers and containers;
- → Busses;
- → Airplanes;
- → Mineral interests;
- → Conservation easements.

Who Benefits from LKEs:

Small business owners and entrepreneurs;
Real estate investors;
Conservationists;
Construction companies and other capital asset intensive businesses;
Farmers and ranchers;
Transportation companies;
Oil and gas companies;
Equipment and vehicle rental and leasing businesses.

Key LKE Provisions:

The properties being exchanged must be held for investment or for use in a trade or business.
The property being exchanged cannot be a primary residence or a personal use property.
The properties must be "like-kind" to each other.
The new property must be identified within 45 days from the date the old property is transferred.
The proceeds from the transfer of the old property must be used to acquire new property within 180 days of the transfer of the old property.
The investor cannot receive the cash from the transfer of the old property.
The transaction must be structured as an exchange of one property for another.

Assets that Cannot be Exchanged:

Stock in trade or other property held primarily for sale (i.e.: inventory);
Stocks, bonds, notes, securities or other debt instruments;

Partnership interests;
Certificates of trust or beneficial interests in trusts.

Examples of Utilization of LKEs:

Farming:

A farmer in Iowa exchanges a distant parcel of land for a larger piece of agricultural property that is contiguous to his home farm. The farmer will not be required to recognize gain on the transfer of the old farm. The farmer does not receive cash from the transfer but receives like-kind property that he continues to hold for investment.

Small Business:

A family business owns and operates a rental car operation in Pennsylvania. As the car fleet ages the business trades-in the old cars for newer models. When the vehicles are exchanged no tax is due. The exchanges allow the company to hire additional staff and to re-deploy their capital into improvements for the business.

Construction:

A construction company is involved in the construction of office buildings. Its operations include concrete pouring, site preparation, plumbing, and electrical work. As their construction equipment ages, the company trades their aged equipment for new equipment. The company does not have to pay tax on the exchange of its equipment and so is able to use its profits to expand its business and grow its workforce.

Commercial Real Estate:

A family owns a multi-unit building in New Jersey. The family lives in one unit and rents out the others. The income from the building allows the family to fund their children's education. When real estate values increase the family exchanges the multi-unit building for a larger building. The tax on the exchange is not currently recognized. With the increased cash flow the family is able to improve the new property providing value to the community.

Conservation:

A rancher in Montana owns 100 acres of environmentally sensitive land that is home to endangered wildlife. A conservancy group offers to buy a permanent conservation easement from the rancher so the land will be protected and the wildlife will flourish. The farmer exchanges the conservation easement for less sensitive, more productive ranchland that he can use to expand his asset and earning base while not infringing on an environmentally sensitive area.