

**New York State Department of Taxation and Finance  
Office of Counsel**

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. M150511A

The Department of Taxation and Finance received a Petition for Advisory Opinion from CDEC LLC, 135 South LaSalle St., Suite 1940, Chicago, IL 60603. Petitioner asks whether a conveyance of real property from an "exchange accommodation titleholder" ("EAT") to a taxpayer as part of a "reverse" like-kind exchange under 26 U.S.C. ("IRC") § 1031 is subject to real estate transfer tax (RETT) under Tax Law § 1402. In this Advisory Opinion, the Petitioner is an EAT. The taxpayer is referred to as the "exchangor."

We conclude that the conveyance of real property from an EAT to the exchangor as part of a "reverse" like-kind exchange under the facts below is not subject to RETT.

**Background and Facts**

IRC § 1031 permits an exchangor to defer current recognition of gain on the sale of property ("relinquished property") for federal income tax purposes to the extent that the exchangor exchanges such property for other property of a "like-kind" ("replacement property"). Both the relinquished property and the replacement property covered by this section must be held for productive use in a trade or business or for investment. Under IRC § 1031(a)(3), an exchangor that sells relinquished property must identify replacement property within 45 days from the disposition of the relinquished property and acquire the replacement property within 180 days from the disposition of the relinquished property. The regulations codified at 26 CFR § 1.1031(k)-1 (the "Regulations") provide guidance and safe harbors for deferred exchanges. Among other things, the Regulations allow for the use of a "qualified intermediary" ("QI"), an independent third party who facilitates the deferred like-kind exchange.

The federal statutes and regulations do not address a "reverse" like-kind exchange ("reverse exchange"), wherein an exchangor acquires replacement property prior to the sale of the relinquished property. In 2000 and 2004, the Internal Revenue Service ("IRS") promulgated Revenue Procedures 2000-37 and 2004-51 (collectively, the "Rev. Procs."), which set forth the criteria for a reverse exchange to qualify for the deferred gain without disturbing the deferred exchange safe harbors in the Regulations. The Rev. Procs. provide for the use of an "exchange accommodation titleholder" ("EAT"), a person or entity independent from the exchangor, to facilitate a reverse exchange by arranging for the acquisition of the replacement property before the exchangor disposes of the relinquished property. Petitioner is in the business of acting as an EAT. Petitioner's affiliate is in the business of acting as a QI.

The Rev. Procs. provide a safe harbor that allows an exchangor to treat the EAT as the owner of the property for federal income tax purposes, thereby enabling such exchangor to accomplish a qualifying reverse like-kind exchange.<sup>1</sup>

Under the Rev. Procs. safe harbor, the IRS will not challenge (a) the qualification of property as either "replacement property" or "relinquished property" for purposes of IRC § 1031 and the regulations thereunder, or (b) the treatment of an EAT as the beneficial owner of property for federal income tax purposes, if the property is held pursuant to a qualified exchange accommodation arrangement ("QEAA").<sup>2</sup> Property is considered to be held in a QEAA if the requirements in Rev. Proc. 2000-37 § 4.02 are met. The requirements are:

(1) Qualified indicia of ownership of the property is held by an EAT who is subject to federal income tax. Such qualified indicia of ownership must be held by the EAT at all times from the date of acquisition by the EAT until the property is transferred. "Qualified indicia of ownership" means legal title to the property, other indicia of ownership of the property that are treated as beneficial ownership of the property under applicable principles of commercial law (*e.g.*, a contract for deed), or interests in an entity that is disregarded as an entity separate from its owner for federal income tax purposes (*e.g.*, a single member limited liability company) and that holds either legal title to the property or such other indicia of ownership;

(2) At the time the qualified indicia of ownership of the replacement or relinquished property is transferred to the EAT, it is the exchangor's bona fide intent that the property held by the EAT represents either replacement property or relinquished property in an exchange that is intended to qualify for nonrecognition of gain or loss under IRC § 1031;

(3) No later than five business days after the transfer of qualified indicia of ownership of the property to the EAT, the exchangor and the EAT must enter into a qualified exchange accommodation agreement (an "accommodation agreement") specifying that the EAT is holding the property for the benefit of the exchangor in order to facilitate the § 1031 exchange and that the EAT will be treated as the beneficial owner of the property for all federal income tax purposes. Both parties must report the federal income tax attributes of the property on the federal income tax returns, consistent with the accommodation agreement;

(4) No later than 45 days after the transfer of qualified indicia of ownership of the replacement property to the EAT, the relinquished property must be properly identified;

(5) No later than 180 days after the transfer of qualified indicia of ownership of the property to the EAT, (a) the replacement property (directly or through a QI) is transferred to the exchangor, or (b) the relinquished property is transferred to a person who is not the exchangor; and

(6) The combined time period that the relinquished property and the replacement property are held in a QEAA does not exceed 180 days.

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<sup>1</sup> Rev. Proc. 2000-37 § 2.06 and Rev. Proc. 2000-37 § 1.

<sup>2</sup> Rev. Proc. 2000-37 § 1.

In a typical accommodation agreement used by the Petitioner, the parties agree that the EAT is acting solely as the exchangor's agent for all purposes except for federal income tax and, as appropriate, state income tax purposes, when the EAT purchases the replacement property and when the EAT conveys the property to the exchangor. During the interim (called "the Parking Period"), the exchangor is solely responsible for all activities, actions, and decisions relating to the management, repair, construction of improvements, insurance, collection of rents and the payment of taxes, mortgage payments, etc. The exchangor indemnifies and holds harmless the EAT and its related entities from all losses, liabilities, fees, expenses, and damages related to the EAT's obligations under the QEAA.

The following are the steps taken in a typical reverse exchange.

A. The Replacement Property: (1) The exchangor and EAT first enter into an accommodation agreement to effectuate a reverse exchange, pursuant to which EAT is acting as exchangor's agent for all purposes except for federal income tax and, as appropriate, state income tax purposes. (2) The exchangor contracts to buy the replacement property and assigns its rights under the contract to the EAT. (3) The EAT then closes on the property and acquires the legal title directly or through a disregarded entity such as a single member limited liability company.

The exchangor provides the EAT with all funds needed to acquire the property (the "Loan"). The EAT is not required to advance or expend any of its own funds. Under the accommodation agreement, the EAT will receive a fee, be reimbursed for all its costs incurred with respect to ownership of the replacement property and transfer the replacement property to the exchangor at no gain or loss. Consistent with the principle that the EAT is merely acting as an agent for the exchangor, the EAT's only financial reward (or risk) under the accommodation agreement is its fee. The EAT does not share in the up- or down-side of fluctuations of the value of the replacement property, or share in its revenues or suffer its costs. In order to keep the EAT economically neutral with respect to the replacement property during the Parking Period, the EAT, as fee owner, will execute a master triple-net lease of the property to the exchangor as master lessee (the "Lease Agreement"). The income and expenses reported by the EAT during the Parking Period are designed to be a wash. Under the Lease Agreement, the amount of the rent due from the exchangor is set equal to the outstanding monthly interest obligation of the EAT under the Loan. Therefore, for federal income tax purposes, the EAT would report rental income and claim a matching deduction for interest paid to the exchangor under the Loan. (4) Real estate transfer taxes are paid on the conveyance of the replacement property to the EAT.

B. The Relinquished Property: (1) The exchangor enters into a purchase and sale contract for the relinquished property with a purchaser. (2) Pursuant to an "exchange agreement," the exchangor assigns its rights (but not its obligations) in the purchase and sale contract for the relinquished property to the QI. The QI's rights in the purchase and sale contract for the relinquished property are subject to the right of the purchaser to acquire the relinquished property. (3) At the QI's direction, the exchangor transfers the relinquished property directly to the purchaser. (4) Real estate transfer taxes are paid on the conveyance of the relinquished property to the purchaser. (5) The QI places the proceeds of the sale in a trust account for the benefit of the exchanger (referenced below as "the trust account").

C. The Exchange: Through the QI, the exchangor has effectuated selling the relinquished property to the purchaser (as described in paragraph B above). Next, the EAT will purchase the



replacement property with funds supplied by the exchangor as one or more nonrecourse loans. The loans will consist of funds advanced by the exchangor, including loans provided by one or more third-party lenders arranged by the exchangor and secured by the replacement property. The EAT will not be expected to pay any costs directly unless the exchangor has provided the funds to the EAT in advance. The exchangor assigns its rights for the replacement property under the QEAA to the QI. Alternatively, the exchanger contracts to purchase from the EAT (i) the replacement property or (ii) the ownership interest in the disregarded entity of the EAT that holds the title to the replacement property. Then, the exchangor assigns its rights to acquire the replacement property under such contract to the QI. Under either scenario, QI buys the replacement property from the EAT with the funds from the trust account and the EAT transfers the replacement property directly to the exchangor. The EAT repays the exchangor any portion of the loans not funded by third-party lenders, and any mortgage is either extinguished or transferred along with the replacement property. As a federal income tax matter, the exchangor is considered to have exchanged the relinquished property for the replacement property, although the EAT acquired the replacement property on the exchangor's behalf prior to the sale of the relinquished property.

### **Analysis**

Tax Law § 1402(a) imposes the RETT on each conveyance of real property or interest therein when the consideration exceeds five hundred dollars. Tax Law § 1401(e) defines "conveyance" as "the transfer or transfers of any interest in real property by any method . . . ." Tax Law § 1401(f) provides, in part, that an "interest in real property" includes a contract to purchase real property, a beneficial interest, and the right to receive rents, profits or other income derived from real property. However, Tax Law § 1405(b)(4) provides that the RETT does not apply to conveyances of real property without consideration and otherwise than in connection with a sale, including conveyances of realty as a bona fide gifts. Tax Law § 1401(d) provides that consideration means the price actually paid or required to be paid for the real property or interest therein, including payment for an option or contract to purchase real property, including discharge of an indebtedness or obligation and the amount of any mortgage or lien.

In a reverse like-kind exchange, there are only two conveyances for consideration: (1) the sale of the replacement property to the EAT that obtains legal title directly or acquires the title indirectly through its ownership of its disregarded entity, and (2) the transfer of the relinquished property from the QI to the purchaser. The sole purpose of the intermediate conveyances to the EAT and the QI is to conform the timing of the transfer of the relinquished property to a buyer, and the acquisition of the replacement property by the exchangor, to the structure required for a like-kind exchange under IRC § 1031. Under the QEAA, the EAT is in substance the agent or nominee of the exchangor. The QEAA provides that all the property held by the EAT is being held for the benefit of the exchangor in order to facilitate the like-kind exchange and that the parties agree that the EAT is acting solely as the exchangor's agent for all purposes except for federal, and as appropriate, state income taxes. The EAT does not use any of its own funds to pay for the acquisitions of the properties, nor does it hold any responsibilities with regard to maintenance of the property. The EAT is paid only its fees for services and, except for the limited responsibilities to pay income taxes on those fees, it is held harmless in all other respects. If, after acquisition of the replacement property, the EAT leases the property to the exchangor prior to the conclusion of the exchange, the exchangor's rent paid to the EAT would equal any payment made by the EAT on a mortgage that secures a loan for the purchase price. Thus, the EAT remains economically neutral

under the terms of the QEAA. The EAT does not report gain or loss from the purchase or sale of the properties. Because the EAT is serving as the agent or nominee for the exchangor, no consideration is provided for the conveyance from the EAT to the exchangor. As such, we conclude that this conveyance is exempt from RETT under § 1405(b)(4).

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DEBORAH R. LIEBMAN  
Deputy Counsel

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.