

REVERSE EXCHANGES

AN OVERVIEW



A Reverse Exchange, also called a “Parking Arrangement”, is a planning tool that allows a Taxpayer some flexibility when structuring a 1031 exchange transaction. “Reverse Exchange” is really a misnomer because a Taxpayer cannot acquire Replacement Property prior to the disposition of Relinquished Property – a Taxpayer must always dispose of Relinquished Property before acquiring Replacement Property.

In a Parking Arrangement, Relinquished Property or Replacement Property is transferred to an Exchange Accommodation Titleholder (EAT), allowing the 1031 exchange to proceed in the correct order.

A Replacement Property Parking Arrangement (Exchange Last) can be utilized when Replacement Property must close prior to the time Relinquished Property is scheduled to close. Replacement Property can be parked with the EAT for up to 180 days. This gives a Taxpayer time to dispose of Relinquished Property in a Forward Exchange through a Qualified Intermediary (QI). Once Relinquished Property closes, the QI then acquires the parked Replacement Property from the EAT and transfers it to the Taxpayer.

In a Relinquished Property Parking Arrangement (Exchange First), Replacement Property must close, but a Taxpayer either does not have a Buyer for Relinquished Property, or the Buyer is not ready to close. In this scenario, a Taxpayer disposes of Relinquished Property by transferring it to the EAT. The Taxpayer then acquires Replacement Property from the third party seller through the QI.

The Service issued guidance on Reverse Exchanges in 2000. Revenue Procedure 2000-37 (effective September 15, 2000) provides a safe harbor under which the Service will not challenge the qualification of Relinquished Property or Replacement Property in certain “Reverse Exchanges”.

Significant planning opportunities are available as a result of the Revenue Procedure 2000-37, including the ability to treat the EAT as the owner of property for federal income tax purposes, and the Taxpayer as the owner of the property for financial reporting and GAAP purposes.