

DO VACATION AND SECOND HOMES QUALIFY FOR IRC §1031 TREATMENT?

It has been established that vacation or second homes held by the Exchanger primarily for personal use do not qualify for tax deferred exchange treatment under IRC §1031. There has been no clear direction when a second home has mixed use, what proportion of rental versus personal use would qualify the property as held in a trade or business. Neither has there been clear direction when a second home qualifies as held for investment. In *Moore v. Commissioner*, T.C. memo 2007-134, the Tax Court held that properties held for personal use with the mere hope or expectation of gain did not establish investment intent.

The IRS issued Revenue Procedure 2008-16, providing safe harbors effective March 10, 2008, under which the IRS will not challenge whether a dwelling unit that is either a relinquished property or a replacement property in a §1031 exchange qualifies as property held for use in a trade or business or for investment purposes. A dwelling unit is defined as “real property improved with a house, apartment, condominium, or similar improvement that provides basic living accommodations including sleeping space, bathroom and cooking facilities.”

The safe harbor for a second home to qualify as relinquished property in a §1031 exchange requires the Exchanger to have owned it for twenty-four months immediately before the exchange, and within each of those 12-month periods the Exchanger must have 1) rented the unit at fair market rental for fourteen or more days, and 2) restricted personal use to the greater of fourteen days or ten percent of the number of days that it was rented within that 12-month period.

In addition, the safe harbor for a second home to qualify as replacement property in a §1031 exchange requires the Exchanger to own the vacation home for twenty-four months immediately after the exchange, and for each of those 12-month periods the Exchanger must 1) rent the unit at fair market rental for fourteen or more days, and 2) restrict personal use to the greater of fourteen days or ten percent of the number of days it was rented within that 12-month period.

BRIEF EXCHANGES

Investment Property Exchange Services, Inc. cannot provide advice regarding specific tax consequences. Investors considering an IRC §1031 tax deferred exchange should seek the counsel of their accountant and attorney to obtain professional and legal advice. © 2007 Investment Property Exchange Services, Inc.