

Funds Used During Exchanges of Like-Kind Property

On May 8, 2006, the Office of Advocacy sent a comment letter to the Department of Treasury (Treasury) and Internal Revenue Service (IRS), in response to their notice of proposed rulemaking entitled, *Escrow Accounts, Trusts and Other Funds Used During Exchanges of Like-Kind Property* (71 Fed. Reg. 6231 February 7, 2006). Advocacy has advised Treasury and IRS to publish in the *Federal Register* an amended initial regulatory flexible analysis (IRFA). A copy of Advocacy's letter to Treasury and IRS can be accessed at <http://www.sba.gov/advo/laws/comments>.

- The Internal Revenue Code (Code) allows taxpayers to engage in like-kind exchanges of business property under section 1031. The use of a Qualified Intermediaries (QI) is a safe harbor that permits taxpayers to complete a deferred like-kind exchange.
- QIs hold the proceeds of a sale of business property while the taxpayer locates replacement business property. In general, QIs generate revenue by charging a fee and retaining all or a portion of the interest earned on the exchange proceeds that they manage. The revenue earned from interest accounts for a significant amount of the QIs overall revenue.
- The Treasury and IRS have proposed treating the funds held by QIs as a loan from the exchanging taxpayer to the QI. If the QI does not remit the entire earnings on the funds they manage to the exchanging taxpayer, then the Treasury and IRS will deem the transaction to be a below market rate loan, which triggers imputed interest at a rate equal to the 182-day Treasury bill.
- According to an industry survey, small business QIs rely on the interest earned on the funds they manage for a significant percentage of their total revenue.
- The proposed rule contained an IRFA, which simply requested economic impact analysis and less burdensome alternatives without providing this information for the regulated industry to respond. Advocacy explained the importance of a complete IRFA and encouraged Treasury and IRS to publish an amended IRFA in the *Federal Register* for public comment.

For more information, visit Advocacy's Webpage at <http://www.sba.gov/advo>, or contact assistant chief counsel Candace B. Ewell by phone at (202) 401-9787 or by email at Candace.Ewell@sba.gov.