



BOARD OF GOVERNORS  
OF THE  
**FEDERAL RESERVE SYSTEM**  
WASHINGTON, D. C. 20551

SCOTT G. ALVAREZ  
GENERAL COUNSEL

February 9, 2006

Debra L. Barbin, Esq.  
Gary Steven Findley & Associates  
1470 North Hundley Street  
Anaheim, California 92806

Dear Ms. Barbin:

You have requested the opinion of the Board's staff, pursuant to section 225.27 of the Board's Regulation Y (12 C.F.R. 225.27), regarding the permissibility of certain proposed activities by The Bank Holdings, Reno, Nevada. The Bank Holdings, a bank holding company, proposes to acquire a subsidiary (the "1031 exchange subsidiary") that provides services to customers seeking to make exchanges of real property pursuant to section 1031 of the Internal Revenue Code ("1031 exchange transactions").

Section 1031 of the Internal Revenue Code provides a U.S. taxpayer with deferral of gain when the taxpayer exchanges his or her property for another property of a "like kind." In a "forward" 1031 exchange transaction, the taxpayer first sells his or her existing property and later purchases a replacement property.<sup>1</sup> In order to complete a forward 1031 exchange transaction successfully, a taxpayer must satisfy certain conditions in section 1031 of the Internal Revenue Code and the U.S. Treasury regulations that implement section 1031. For

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<sup>1</sup> In a "reverse" 1031 exchange transaction, the taxpayer first purchases a replacement property and later sells his or her property. Your proposal does not include the provision of services to customers seeking to make reverse 1031 exchange transactions.

example, in a forward 1031 exchange transaction, at the closing of the sale of the initial property, the proceeds of the sale must be held by an individual or entity otherwise unrelated to the transaction (the “qualified intermediary”). In addition, the taxpayer engaging in the forward 1031 exchange transaction may not receive the sale proceeds during the period in which a replacement property is identified (up to 45 days) and acquired (up to 180 days). The Bank Holdings proposes to acquire a subsidiary that will act as a qualified intermediary in forward 1031 exchange transactions involving real property.

The 1031 exchange subsidiary would engage in several activities in order to facilitate forward 1031 exchange transactions. First, the subsidiary would provide its customer with documents related to the exchange in order to ensure that the exchange qualifies as a valid forward 1031 exchange transaction. Specifically, the subsidiary would provide a form of exchange agreement, assignment agreement, and notice. The exchange agreement is a contract between the customer and the subsidiary that, among other features, notes the requirements for the successful completion of the transaction. The assignment agreement transfers from the customer to the subsidiary certain responsibilities for the sale of the initial property and the receipt of sales proceeds in order to ensure that the customer does not “constructively receive” the proceeds of the initial property sale for tax purposes. These responsibilities may include taking transitory title to the initial property and the replacement property as they are transferred from seller to buyer. The notice informs the purchaser of the initial property that the transaction is part of a forward 1031 exchange transaction in order to help establish that the mechanism for the forward 1031 exchange transaction was in place at the time of the sale.

Second, the 1031 exchange subsidiary would invest the proceeds of the sale of the initial property on behalf of the customer until the customer acquires the replacement property. The proceeds would be invested at the discretion of the subsidiary, but would typically be deposited into deposit accounts at Nevada Security Bank, Reno, Nevada, the subsidiary commercial bank of The Bank Holdings.<sup>2</sup> The subsidiary would also transfer the necessary

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<sup>2</sup> Nevada Security Bank may also be a lender with respect to the real properties involved in the 1031 exchange transaction. Any lending relationship between the bank and the customer would depend upon the ability of the customer and the loan transaction to meet the bank’s standard underwriting terms and conditions.

funds to the appropriate party to effect the customer's purchase of the replacement property. If the customer does not identify a replacement property, or purchase the replacement property, within the required time periods set forth in section 1031 of the Internal Revenue Code or U.S. Treasury regulations implementing section 1031, the proceeds of the sale of the initial property would be transferred to the customer. You have indicated that the subsidiary would act in a fiduciary capacity in holding, investing, and disbursing the customer's funds and that a nondepository trust company chartered by the State of Nevada would be allowed to engage in the activities of the subsidiary.

The 1031 exchange subsidiary will not participate in negotiating the terms of the real property sale and purchase transactions that constitute the forward 1031 exchange transaction and will not assist the customer in locating a buyer of the initial property or a seller of the replacement property.

You contend that the proposed services are permissible nonbanking activities for bank holding companies described in section 225.28(b) of Regulation Y (12 C.F.R. 225.28(b)).

In view of all the facts of record, it is my opinion that the proposed activities of the 1031 exchange subsidiary are permissible real estate settlement services under section 225.28(b)(2)(viii) of Regulation Y (12 C.F.R. 225.28(b)(2)(viii)); trust company functions under section 225.28(b)(5) of Regulation Y (12 C.F.R. 225.28(b)(5)); and financial advisory services, including tax planning and tax preparation services, under section 225.28(b)(6) of Regulation Y (12 C.F.R. 225.28(b)(6)).<sup>3</sup>

This opinion is limited solely to the 1031 exchange facilitation activities described above and in your correspondence with Board staff. Any material change in the proposed activities could result in a different conclusion

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<sup>3</sup> The Office of the Comptroller of the Currency has authorized national banks to provide a wide range of services to facilitate customer 1031 exchange transactions. See OCC Interpretive Letter No. 880 (December 16, 1999); OCC Corporate Decision No. 2001-30 (October 10, 2001).

and should be reported to Board staff. If you have any questions regarding this matter, please contact Mark E. Van Der Weide (202/452-2263) or Michael Waldron (202/452-2798) of the Board's Legal Division.

Sincerely,

*[signed Scott G. Alvarez]*

cc: Federal Reserve Bank of San Francisco