

Farm and Ranch Exchanges

Farm and ranch exchanges present a host of opportunities and challenges for taxpayers since they often include a mix of different assets with differing requirements and concerns under Code Section 1031. In a nutshell, here are some of the issues involved in farm and ranch exchanges.

Real Estate can be exchanged for like-kind real estate held for business or investment and in most cases is without complication. A sale of “real estate” can include a variety of real estate interests which all qualify as “real estate” under the like-kind replacement rules, including –

- Fee simple ownership
- 30+ year leasehold interests
- Water and mineral rights
- Conservation and use rights
- Grazing rights

Equipment included in the sale-exchange can be replaced with like-kind equipment. For farmers, almost any farm equipment qualifies as like-kind. The like-kind rules for farm equipment are described in the General Asset Classes of Regulation §1.1031(a)-2(b)(2) and the Product Classes of Sector 33 of the North American Industry Classification System (NAICS).

Center Pivot Sprinkling Systems are usually assumed to be subject to the like-kind replacement rules for equipment. But, there is an argument that a center pivot sprinkler system qualifies as a real estate improvement and, accordingly, can qualify under the like-kind rules applying to real estate when a taxpayer is replacing with real estate with sprinkler equipment on it. This won't work if the farm that is being sold has a sprinkler system on it and is being exchanged for land without a sprinkler system. In this case Section 1245 depreciation recapture would kick-in if the sprinkler being sold is not replaced with Section 1245 equipment. Farm and ranch owners with sprinkling equipment need to consider these issues and discuss with their tax professional for exchange planning.

Breeding or Dairy Livestock can be exchanged for “like-kind livestock.” Same-sex is required under the like-kind rules; a bull cannot be exchanged for a heifer or cow and vice versa. Steers or feeder stock don't qualify.

Personal Residence Issues are often a part of an exchange of farm or ranch property. If the owner lives in a personal residence on the farm the gain allocable to the personal residence may be tax free under Code Section 121 limited to \$250,000 (single) or \$500,000 (married filing jointly). Preferred practice is to bifurcate the sale into two sales with the taxpayer cashing out on the sale of the personal residence and proceeding with a 1031 Exchange of the balance of the farm sale.

Related Party transactions require special attention in a 1031 Exchange of farm and ranch property. “Related parties” include related individuals and related entities such as corporations, partnerships, LLCs and trusts. Deed swaps between related parties require that each party hold the property for 24 months to validate the exchange. A sale to a related party with replacement from an unrelated party is not considered to be a “related party exchange.” A sale to an unrelated party with replacement from a related party is not permitted if the related party is cashing out. It is permitted if the related party is also going thru a 1031 Exchange with replacement of qualifying real estate. Related parties or entities are described in Code Section 267(b) or 707(b)(1).

Talk to your tax advisor when you are anticipating a sale of farm or ranch property. Call us at 888-367-1031 or email us at 1031@1031cpas.com if we can assist with questions about an exchange of your property. See our Exchange Manual and visit us at www.1031cpas.com. 1031 Corporation is the Intermediary of choice for real estate professionals, CPAs and investors.

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