

**Internal Revenue Service**

Department of the Treasury

Index Number: 932.00-00; 1031.02-00

Washington, DC 20224

Number: **200040017**

Person to Contact:

Release Date: 10/6/2000

Telephone Number:

Refer Reply To:

CC:DOM:IT&amp;A:5-PLR-103258-00

Date:

June 30, 2000

TY:

Legend

Husband	=
Taxpayer	=
City	=
City 2	=
State	=
Bank	=
Year 1	=
Year 2	=
Year 3	=
Year 4	=
Year 5	=

Dear :

This letter is in response to a letter ruling request received by this office on February 7, 2000. Specifically, you have requested the following ruling:

The rental real estate located in the United States Virgin Islands to be received as Replacement Property in the deferred exchange will be treated as like-kind property to the Relinquished Property for purposes of § 1031(a).

**FACTS**

In Year 1, Taxpayer and Husband, both U.S. citizens, acquired a 6-unit commercial building for investment located in City, State. Taxpayer's and Husband's interest in the building was held in a State land trust, with Bank acting as trustee. In Year 2 or Year 3, Husband transferred his beneficial interest in the land trust to Taxpayer, so that Taxpayer held all the beneficial interest in the trust.

In Year 4, Taxpayer contracted to sell the property held in the land trust. The contract is to be assigned to a Qualified Intermediary, as defined in § 1031(k)-1(g)(4) of

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the Income Tax Regulations. For Replacement Properties, Taxpayer (or the land trust as her nominee) intends to acquire one property in City, State, and one located in City 2, U.S. Virgin Islands. It is anticipated that the Replacement Property located in the U.S. Virgin Islands will produce income for the taxable Year 5.

### LAW AND ANALYSIS

Section 1031(a)(1) of the Code provides that no gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.

Section 1.1031(a)-1(a) of the Regulations provides in part that § 1031(a)(1) provides an exception from the general rule requiring the recognition of gain or loss upon the sale or exchange of property.

Section 1.1031(a)-1(b) of the Regulations provides in part that for the purposes of § 1031(a), the words “like kind” have reference to the nature or character of the property, and not to its grade or quality. One kind or class of property may not, under that section, be exchanged for property of a different kind or class.

Section 1031(h) of the Code provides that real property located in the United States and real property located outside the United States are not property of a like kind.

Section 7701(a)(9) of the Code provides that the term “United States” when used in a geographical sense includes only the States and the District of Columbia.

Section 932(a)(1) of the Code provides that this subsection shall apply to an individual for the taxable year if

(A) such individual

(i) is a citizen or resident of the United States (other than a bona fide resident of the Virgin Islands at the close of the taxable year), and

(ii) has income derived from sources within the Virgin Islands, or effectively connected with the conduct of a trade or business within such possession, for the taxable year, or

(B) such individual files a joint return for the taxable year with an individual described in § 932(a)(1)(A).

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Section 932(a)(2) of the Code provides that each individual to whom § 932(a) applies for the taxable year shall file his income tax return for the taxable year with both the United States and the Virgin Islands.

Section 932(a)(3) of the Code provides that in the case of an individual to whom §932(a) applies in a taxable year for purposes of so much of this title (other than this section and § 7654) as relates to the taxes imposed by this chapter, the United States shall be treated as including the Virgin Islands.

Rev. Rul. 92-105, 1992-2 C.B. 204, provides that a taxpayer's interest in an Illinois land trust constitutes real property which may be exchanged for other real property without recognition of gain or loss under § 1031 of the Code, provided the requirements of that section are otherwise satisfied. This ruling is not applicable if an arrangement involving an Illinois land trust creates an entity (such as a partnership). State is a state that has laws authorizing land trust arrangements that satisfy the requirements of Rev. Rul. 92-105. Thus, Taxpayer's interest in a State land trust constitutes real property for purposes of § 1031.

The legislative history of § 1031(h) indicates that it was the intent of Congress that "no inference is intended to override or otherwise modify § 932 of the Code (involving the tax treatment of U.S. and Virgin Islands residents)." H.R. Rep. No. 386, 101<sup>st</sup> Cong., 1<sup>st</sup> Sess. 614 (Conference Committee Report 1989). Therefore, if the taxpayer involved in the exchange is a citizen or resident of the United States, and has income derived from sources within the Virgin Islands, or effectively connected with the conduct of a trade or business within such possession, or files a joint return with an individual who meets the foregoing requirements, for the taxable year of the exchange, then § 932(a) applies and the United States is enlarged to include the Virgin Islands.

In the present case, Taxpayer is a citizen of the United States who currently owns investment property in State, which she intends to exchange for investment properties in State and the Virgin Islands. Taxpayer expects the Replacement Property in the U.S. Virgin Islands to produce income in taxable Year 4 in the months following the exchange. Provided that the Replacement Property located in the U.S. Virgin Islands produces income for Taxpayer in Year 4, § 932 will apply, and the United States will be treated as including the Virgin Islands for the purposes of this exchange. Accordingly, § 1031(h) will not apply, since neither of the Replacement Properties will be outside the United States. Therefore, we rule that the Replacement Property located in the U.S. Virgin Islands consisting of rental real estate is like kind to the Relinquished Property for purposes of § 1031, provided that this Replacement Property produces income in Year 4.

Except as is specifically ruled above, no opinion is expressed as to the federal tax treatment of the transaction under the provisions of any other section of the Internal Revenue Code and regulations thereunder. No opinion is expressed as to the tax

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treatment of any conditions existing at the time of or effects resulting from the transaction that is not specifically covered by the above rulings.

A copy of this letter should be attached to the appropriate federal income tax return for the taxable year in which the transaction herein described is consummated.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,  
Kelly E. Alton  
Senior Technician Reviewer, Branch 5  
Income Tax and Accounting