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December 14, 2020

The Honorable Chuck Grassley
Chairman
The Honorable Ron Wyden
Ranking Member
Committee on Finance
United States Senate

The Honorable Richard Neal
Chairman
The Honorable Kevin Brady
Ranking Member
Committee on Ways and Means
House of Representatives

Subject: *Department of the Treasury, Internal Revenue Service: Statutory Limitations on Like-Kind Exchanges*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Department of the Treasury, Internal Revenue Service (IRS) entitled “Statutory Limitations on Like-Kind Exchanges” (RIN: 1545-BP02). We received the rule on December 3, 2020. It was published in the *Federal Register* as final regulations on December 2, 2020. 85 Fed. Reg.77365. The final rule has an effective date of December 2, 2020.

According to IRS, the final rule provides guidance under section 1031 of the Internal Revenue Code (Code), 26 U.S.C. § 1031, to implement recent statutory changes to that section. IRS stated the final rule amends the current like-kind exchange regulations to add a definition of real property to implement statutory changes limiting section 1031 treatment to like-kind exchanges of real property. IRS further stated the final rule also provides a rule addressing a taxpayer’s receipt of personal property that is incidental to real property the taxpayer receives in an otherwise qualifying like-kind exchange of real property. IRS also stated the final rule affects taxpayers that exchange business or investment property for other business or investment property and that must determine whether the exchanged properties are real property under section 1031.

The Congressional Review Act (CRA) requires a 60-day delay in the effective date of a major rule from the date of publication in the *Federal Register* or receipt of the rule by Congress, whichever is later. 5 U.S.C. § 801(a)(3)(A). The 60-day delay in effective date can be waived, however, if the agency finds for good cause that delay is impracticable, unnecessary, or contrary to the public interest, and the agency incorporates a statement of the findings and its reasons in the rule issued. 5 U.S.C. § 808(2). IRS determined it had good cause to waive the

delay. According to IRS, following the amendments to section 1031, the Treasury Department and IRS published a proposed rule to provide certainty to taxpayers. IRS stated that, as emphasized by the wide variety of public comments received in response to the proposed rule, taxpayers lacked certainty regarding the longstanding role of state and local law in real property determinations for purposes of qualification under section 1031. Because of this, the Treasury Department and IRS have determined that an expedited effective date of the final rule would give businesses, especially small businesses, the confidence they need to re-open by providing guidance on what the law requires.

Enclosed is our assessment of IRS's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shari Brewster, Assistant General Counsel, at (202) 512-6398.

A handwritten signature in black ink that reads "Shirley A. Jones". The signature is written in a cursive, flowing style.

Shirley A. Jones
Managing Associate General Counsel

Enclosure

cc: Carrie E. Mudd
Director, Legal Processing Division
Department of the Treasury:

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ENTITLED
"STATUTORY LIMITATIONS ON LIKE-KIND EXCHANGES
(RIN: 1545-BP02)

(i) Cost-benefit analysis

The Department of the Treasury, Internal Revenue Service (IRS) estimated that using the final rule's local law test and eliminating the purpose or use test that was included in the proposed rule will reduce compliance costs relative to the proposed rule. IRS stated taxpayers may rely on existing state and local law definitions of real property or may look to the specifically listed property or the various factors provided in the final rule. IRS also stated the final rule may influence which intangible assets qualify as real property for like-kind exchanges relative to the definition in the proposed rule.

With regard to a limitation on the value of incidental personal property in excess of 15 percent, IRS determined that a higher limit might induce taxpayers to bundle more personal property with their exchanged property. According to IRS, such a result would lead to increased amounts of personal property exchanged with real property under section 1031 of the Internal Revenue Code, 26 U.S.C. § 1031, and effectively unlock a class of personal property that would no longer be "incidental" to the real property. With regard to a lower limit, IRS further determined that the burden of accurately measuring the separate costs of comingled personal and real property would increase. In addition, IRS estimated the final 15 percent incidental personal property limitation would reduce the cost of investing in real property, when compared to no exchanges for incidental personal property.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

IRS certified the final rule would not have a significant economic impact on a substantial number of small entities.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

IRS determined the final rule does not include any mandate that may result in expenditures in any one year by state, local, or tribal governments, or by the private sector in excess of \$156 million (\$100 million, adjusted for inflation).

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

On June 12, 2020, IRS published a proposed rule. 85 Fed. Reg. 35835. IRS received 21 comments to the proposed rule and addressed them in the final rule.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

IRS determined the final rule contains information collection requirements (ICRs) subject to the Act. The ICR is entitled Form 8824, Like-Kind Exchanges and is associated with Office of Management and Budget (OMB) Control Number 1545-0074. IRS stated no burden estimates specific to the final rule are currently available.

Statutory authorization for the rule

IRS promulgated the final rule pursuant to section 7805 of title 26, United States Code.

Executive Order No. 12866 (Regulatory Planning and Review)

IRS stated the final rule was designated economically significant and was reviewed by OMB.

Executive Order No. 13132 (Federalism)

IRS determined the final rule does not have federalism implications and does not impose substantial, direct compliance costs on state and local governments or preempt state law.