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Department of the Treasury

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:ITA:B05

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August 30, 2004

DO:

Dear _____ :

This letter responds to your request for two rulings. First, you have requested a ruling that sport utility vehicles ("SUVs") will be treated as like kind to passenger automobiles for purposes of section 1031 of the Internal Revenue Code ("Code") and the regulations thereunder. Second, you have requested a ruling that the deferred like-kind exchange program implemented by Subsidiary meets the assignment safe harbor and notice requirements in section 6.02 of Rev. Proc. 2003-39, 2003-22 IRB 971.

FACTS

Subsidiary is wholly owned by Taxpayer. Taxpayer and Subsidiary file a consolidated return. Subsidiary is primarily engaged in the business of leasing vehicles to consumers and issuing loans to consumers for the purchase of vehicles. Leases are originated through a national network of independent dealers of Taxpayer's vehicles. Following the standard industry practice, customers are commonly given the option of either leasing or purchasing a new vehicle from the dealer. When a customer desires to lease a new vehicle, the dealer offers to initiate a lease on behalf of Subsidiary. Subsidiary regularly disposes of leased vehicles and replaces them with new vehicles as lease term expiration and customer demand require. Subsidiary currently maintains a portfolio of vehicles leased to customers. These vehicles include automobiles and sport utility vehicles ("SUVs").

Subsidiary has implemented a deferred like-kind exchange program ("LKE Program") for these vehicles. Consequently, Subsidiary has structured its vehicle leasing operations with the intention that the disposition of a vehicle coming off lease (a relinquished vehicle) by Subsidiary to an unrelated party and the acquisition by Subsidiary of a vehicle recently leased from a dealer (a replacement vehicle) will qualify as a like-kind exchange under section 1031. Relinquished vehicles are typically sold to the dealer, the lessee, or at auction to a third party. Replacement vehicles are usually purchased from a member of the dealer network.

The LKE Program is an ongoing program involving multiple exchanges of 100 or more vehicles. To meet the requirements of section 1031, Subsidiary entered into an Exchange Agreement with QI, under which QI is to act as a qualified intermediary under section 1.1031(k)-1(g)(4) of the Income Tax Regulations.

QI maintains different types of accounts for Subsidiary: Collection Accounts; Concentration Accounts; Disbursement Accounts and Investment Accounts. The Collection Accounts hold amounts received by QI from the sale of relinquished vehicles as well as other receipts. Those amounts related to the LKE Program are transferred to the Concentration Accounts by the QI. Each day, funds from the sale of relinquished vehicles are transferred by the QI from the Concentration Accounts to the Disbursement Accounts in order to fund the acquisition of replacement vehicles from dealers. All amounts expended by QI in the acquisition of vehicles are funded by disbursements directly from the Disbursement Accounts by check or electronic funds transfer.

Under the Exchange Agreement, Subsidiary makes a master assignment to QI of its rights (but not its obligations) in its existing and future agreements to purchase replacement property and to sell relinquished property. In all instances, the seller of replacement property receives written notice prior to the time that the replacement property is transferred to Subsidiary. Notice is provided to dealers in lease agreements, credit approval faxes, and funding approval faxes. The purchasers of relinquished property also receive written notice prior to transfer. Notice is provided to lessees, dealers and third parties in written payoff quotes and, in the case of auction sales, electronic files submitted to the auction house and bills of sale.

LAW AND ANALYSIS

Section 1031(a)(1) of the Code provides that in general, 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(k)-1(a) of the regulations provides that a deferred exchange is defined as an exchange in which, pursuant to an agreement, the taxpayer transfers property held for productive use in a trade or business or for investment (the "relinquished property") and subsequently receives property to be held either for productive use in a

trade or business or for investment (the "replacement property"). In order to constitute a deferred exchange, the transaction must be an exchange (i.e. a transfer of property for property, as distinguished from a transfer of property for money). For example, a sale of property followed by a purchase of property of a like kind does not qualify for nonrecognition of gain or loss under section 1031 regardless of whether the identification and receipt requirements of section 1031(a)(3) and paragraphs (b), (c), and (d) of section 1.1031(k)-1 are satisfied.

Your first ruling request is that SUVs will be treated as like kind to passenger automobiles for purposes of section 1031 of the Code and the regulations thereunder.

Section 1.1031(a)-1(b) provides that as used in section 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 Code section, be exchanged for property of a different kind or class. As an example, section 1.1031(a)-1(c) provides that "a truck for a new truck or a passenger automobile for a new passenger automobile to be used for a like purpose" are like kind.

Section 1.1031(a)-2(b) further provides as a safe harbor that depreciable tangible properties are of like class if they are either within the same General Asset Class, as defined in section 1.1031(a)-2(b)(2), or within the same Product Class, as defined in section 1.1031(a)-2(b)(3).

The General Asset Class and Product Class safe harbors in the regulations simplify the determination of whether depreciable tangible personal property is of a like kind, but they are not the exclusive method for making this determination. For depreciable tangible personal property to be considered of like kind, the property can be either like kind or like class. Section 1.1031(a)-2(a) of the regulations provides that "an exchange of properties of a like kind may qualify under section 1031 regardless of whether the properties are also of like class. In determining whether exchanged properties are of a like kind, no inference is to be drawn from the fact that the properties are not of a like class." Thus, two properties can be in different General Asset Classes (and thus not be of a like class) and yet be of like kind.

The like-kind property standard has been interpreted more narrowly in the case of exchanges of personal property as compared to exchanges of real property. See California Federal Life Insurance Co. v. Commissioner, 680 F.2d 85, 87 (9th Cir. 1982). Even within the more restrictive parameters of the like-kind standard as applied to personal property, the differences between an automobile and an SUV do not rise to the level of a difference in nature or character but are merely a difference in grade or quality. Thus, we conclude that the two are like kind property.

The second ruling you have requested is that the deferred like-kind exchange program implemented by Subsidiary meets the assignment safe harbor and notice requirements in section 6.02 of Rev. Proc. 2003-39, 2003-22 IRB 971.

Section 1.1031(k)-1(g)(4)(iii) requires that, for an intermediary to be a qualified intermediary, the intermediary must enter into a written “exchange” agreement with the taxpayer and, as required by the exchange agreement, acquire the relinquished property from the taxpayer, transfer the relinquished property, acquire the replacement property, and transfer the replacement property to the taxpayer.

Section 1.1031(k)-1(g)(4)(v) provides that an intermediary will be treated as entering into an agreement for the acquisition or transfer of property if the taxpayer’s rights in the agreement are assigned to the intermediary, and the other parties to the acquisition or transfer agreement are notified in writing of the assignment on or before the date of the relevant transfer of property (“Assignment Safe Harbor”). Under the Assignment Safe Harbor, there is no requirement that the taxpayer also assign or delegate its obligations under the agreement.

Rev. Proc. 2003-39 provides certain safe harbors with respect to LKE programs involving ongoing exchanges of tangible personal property using a single intermediary. Section 6.02 of that revenue procedure provides that the taxpayer’s assignment in the master exchange agreement to the intermediary of the taxpayer’s rights (but not necessarily its obligations) in some or all of its existing and future agreements to sell relinquished property and/or to purchase replacement property, and the taxpayer’s written notice of the assignment to the other party to each agreement to sell relinquished property and/or to purchase replacement property on or before the date of the relevant transfer of property, will be effective to satisfy the Assignment Safe Harbor under section 1.1031(k)-1(g)(4)(v).

In the instant case, Subsidiary has assigned to QI its rights to sell the relinquished property. In all instances, the purchaser receives written notice of the assignment prior to the time that the relinquished property is transferred to the purchaser. Notice is provided in written payoff quotes and, in the case of auction sales, electronic files submitted to the auction house and the bills of sale.

In addition, Subsidiary assigned its right to purchase replacement property to QI. In all instances, the seller receives written notice prior to the time that the replacement property is transferred to Subsidiary. Notice is provided to dealers in lease agreements, credit approval faxes, and funding approval faxes.

CONCLUSIONS

Accordingly, based on your representations and the above analysis, we conclude that SUVs and passenger automobiles are like kind property for purposes of section 1031 of the Code and the regulations thereunder. We further conclude that the deferred like-kind exchange program implemented by Subsidiary meets the Assignment Safe Harbor in section 6.02 of Rev. Proc. 2003-39, 2003-22 IRB 971.

CAVEATS

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under 6110 of the Internal Revenue Code.

In accordance with the Power of Attorney on file with this office, copies of this letter are being sent to the Taxpayer's authorized representatives.

The rulings contained in this letter are based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

John M. Aramburu
Senior Counsel, Branch 5
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures (2)