



Who is a Related Party in a 1031 Exchange?

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Who Is Considered a Related Party?

The definition of a related party is the most important issue involved in any [related party](#) 1031 exchange transaction. A related party is not limited just to family members. Related parties can also be C or S corporations, general or limited partnerships, limited liability companies, revocable and irrevocable trusts, as well as other entities. Therefore, related parties generally include certain family members, business entities, and other common ownership or control relationships.

Definition of Related Parties Pursuant to Sections 267(b) and 707(b)(1)

The term “related person,” “related party,” or “[related parties](#)” means any person, party or legal entity, that has a relationship to the exchangor (taxpayer) described in Section 267(b) or Section 707(b)(1) of the IRC, including:

- Members of the same family unit such as siblings, spouse, ancestors (e.g., parents, grandparents, great grandparents), and lineal descendants (e.g., children, grandchildren, great grandchildren);
- A corporation where more than 50% of the value of the stock is owned directly or indirectly by or for one particular individual that is related to the taxpayer;
- Two (2) corporations that are in the same controlled group (as defined in Section 1031, subsection (f));
- A grantor and a fiduciary of any trust;
- A fiduciary of one trust and the fiduciary and/or beneficiary of another trust where the same person is the grantor for both trusts;
- A fiduciary of a trust and a beneficiary of the same trust;
- A corporation where more than 50% of the value of the stock is owned directly or indirectly by or for one particular trust or by or for the grantor or fiduciary of the trust;
- An organization qualified under Section 501 of the Internal Revenue Code (relating to certain educational or charitable non-profit organizations) which is controlled directly or indirectly by a specific person or (if such person is an individual) by members of the family of such individual;
- A corporation and a partnership if the same person or people own:
 - more than 50% in value of the outstanding stock of the corporation, and
 - more than 50% of the capital interest, or the profits interest, in the partnership;
- An S corporation and another S corporation or a C corporation if the same person or persons own more than 50% in value of the outstanding stock of each corporation;
- A partnership and a person owning, directly or indirectly, more than a 50% capital interest or a 50% profits interest, in such partnership;
- Two partnerships in which the same person or persons own, directly or indirectly, more than a 50% capital interest or a 50% profits interest, in both partnerships;
- An executor of an estate and the beneficiaries of the estate; or
- Other relationships described under Internal Revenue Code Sections 267(b) and 707(b).

Investors may be able to eliminate or fix related party transaction problems by changing the ownership of the related party entity such as transferring or disposing of interests in a multiple member limited liability companies, general or limited partnerships or shares of common stock in a C or S corporation to a non-related third-party to get the related party’s ownership percentage so that it does not exceed 50.0%.



Constructive Ownership and Attribution Rules

The constructive ownership, aggregation of ownership or attribution rules under Section 267(c) of the Internal Revenue Code apply in determining the ownership of common stock, capital interests, or profit interests. The analysis can be more complicated than it first appears because these indirect ownership and attribution rules may apply. Investors should not assume that separate legal entities are not related because they have different names, different ownership structures or different employer identification numbers.

Relationships That May Not Always Be Treated the Same Way

Relationships that people often assume are considered to be related parties are not necessarily treated as related parties in the same way under the applicable tax code provisions and corresponding Treasury Regulations. Depending on the facts, these relationships may include:

- In-laws;
- Aunts and uncles;
- Nieces and nephews;
- Cousins;
- Stepparents or stepchildren;
- Former spouses; and
- More distant family relationships.

However, these relationships should still be reviewed carefully. The tax code, regulations, and related rules are technical, and ownership interests, entity structures, trust arrangements, or indirect relationships can change the analysis. A [relationship](#) that appears unrelated at first may still create related party concerns under the applicable rules. It is crucial that you have your legal, tax and financial advisors review transactions for potential related party issues before proceeding.