Legal 1031 Exchange Services, LLC
a Kensington Vanguard Company

Converting 1031 Investment Property to Personal Use

Are you considering selling your investment property in a 1031 exchange for a house in the country, a condo on the coast or a cabin in the woods? The 1031 Exchange Requires the replacement property to be held for "investment intent." The IRS Recognizes that many taxpayers acquire 1031 replacement properties that are intended primarily for investment purposes, but the taxpayer may also use the properties occasionally for personal use.

To help clarify the qualifications of such properties, the IRS issued Revenue Procedure 2008-15 providing taxpayers with a safe harbor under which a residential unit will qualify as investment property for §1031 even though a taxpayer occasionally uses the property for personal use.

The IRS will not challenge whether a residential replacement property qualifies under Section 1031 as property held for investment or held for productive use in a trade or business, if the qualifying use meets the following standards:

(A) The dwelling unit is owned by the taxpayer for at least 24 months immediately after the exchange (the "qualifying use period"); and
(B) Within the qualifying use period, each of the two 12-month periods immediately after the exchange,

  i. The taxpayer rents the dwelling unit at a fair rental for 14 days or more, and

  ii. The taxpayer's personal use of the property does not exceed the greater of 14 days or 10% of the number of days during the 12-month period that the dwelling unit is rented at a fair rental.

The taxpayer should acquire the investment property with the investment property with the intention of meeting such standards. Subsequently, a taxpayer may reassess their use of the replacement property. For example, in year three, after successfully meeting the parameters of Revenue Procedure 2008-16, the taxpayer may decide at such time to cease renting the property and convert the property to a primary residence or vacation home. At that time, the exchanger transaction is well past, and the taxpayer has established their investment intent in accordance with the safe harbor and the conversion of use in the property should not create tax risk. Furthermore, if the property is converted to a primary residence, there is an opportunity upon sale to benefit from IRC 121, the primary residence exemption.

QUALIFIED INTERMEDIARY SERVICES NATIONWIDE

Legal 1031 Exchange Services, LLC

info@legal1031.com

www.legal1031.com

877-701-1031