Click v. Commissioner, 78 T. C. 225 (1982)

A like-kind exchange under section 1031 requires that the property received be held for productive use in a trade or business or for investment.

Summary

Dollie Click exchanged her farmland for two residential properties, cash, and a note, intending to gift the residences to her children. The IRS challenged the exchange's nonrecognition treatment under section 1031, arguing Click lacked investment intent. The Tax Court agreed, ruling that Click's primary intent was to provide homes for her children, not to hold the properties as investments. The decision underscores the necessity of demonstrating investment intent at the time of a like-kind exchange to qualify for tax deferral.

Facts

Dollie Click owned farmland that she exchanged on July 9, 1974, for two residential properties, cash, and a note from Marriott Corp. Her children and their families moved into the residences on the same day. Approximately seven months later, Click gifted the residences to her children. Click reported the exchange on her 1974 tax return as a like-kind exchange under section 1031.

Procedural History

The IRS issued a statutory notice of deficiency to Click on August 4, 1978, for the taxable year 1974. Click paid the deficiency and subsequently filed a petition with the U. S. Tax Court on October 26, 1978, challenging the IRS's determination. The IRS amended its answer on January 13, 1981, increasing the deficiency, and Click amended her petition to request a refund of the paid deficiency and interest.

Issue(s)

1. Whether Click's exchange of farmland for two residential properties, cash, and a note qualifies for nonrecognition treatment under section 1031(a) of the Internal Revenue Code?

Holding

1. No, because Click did not intend to hold the residential properties received for productive use in a trade or business or for investment.

Court's Reasoning

The court focused on the requirement under section 1031 that the property received must be held for investment or productive use. It found that Click's primary intent was to gift the residences to her children, not to hold them as investments. The

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court noted Click's suggestion to her children to find "swap" properties, her estate planning activities around the time of the exchange, and the lack of personal involvement with the properties post-exchange. The court concluded that Click's intent was to provide homes for her children, not to invest in the properties, thus disqualifying the transaction from section 1031 treatment.

Practical Implications

This decision emphasizes the importance of demonstrating a clear intent to hold exchanged property for investment or productive use at the time of the exchange. Attorneys advising clients on like-kind exchanges must ensure that clients can substantiate their investment intent, particularly when personal use of the property by family members is involved. The case also highlights the IRS's scrutiny of exchanges where subsequent gifts are made, suggesting that taxpayers should carefully document their intent and use of exchanged properties to avoid similar challenges.

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