

April 10, 2024

The Honorable Jason Smith  
Chairman  
House Committee on Ways and Means  
1139 Longworth House Building  
Washington, DC 20515

The Honorable Ron Wyden  
Chairman  
Senate Committee on Finance  
219 Dirksen Senate Building  
Washington, DC 20510

The Honorable Richard E. Neal  
Ranking Member  
House Committee on Ways and Means  
1129 Longworth House Building  
Washington, DC 20515

The Honorable Michael D. Crapo  
Ranking Member  
Senate Committee on Finance  
219 Dirksen Senate Building  
Washington, DC 20510

Dear Chairmen Smith and Wyden and Ranking Members Neal and Crapo:

We write to express our strong support for preserving the like-kind exchange rules under Internal Revenue Code Section 1031. Section 1031 is a time-tested provision critical to the health of U.S. commercial real estate and the well-being of communities across the country.

In a like-kind exchange, an investor can elect to defer the taxation of capital gain on the disposition of investment or business-use real property if the taxpayer reinvests the proceeds in another property of a like kind, in a short window of time. The capital formation spurred by section 1031 supports a virtuous cycle of job-creating reinvestment in American communities. In so doing, like-kind exchanges increase economic mobility for cash-poor small business owners, farmers, and entrepreneurs—including minorities, women, and veterans—while contributing to environmental conservation efforts, housing affordability, and redevelopment in economically struggling cities and towns. We respectfully urge you to reject proposals to restrict section 1031, such as those included in President Biden’s FY 2025 Budget.

**In the post-pandemic economy, like-kind exchanges are more important than ever to the health, recovery, and realignment of U.S. commercial real estate.** By allowing the deferral of tax when one property is exchanged for another, like-kind exchanges help get real estate into the hands of new owners with the time, resources, and desire to restore and improve them. This is particularly important given the need to repurpose or renovate many properties, particularly in the office, retail and hotel sectors, to meet post-pandemic needs. Without section 1031, many of these properties would languish—underutilized and underinvested—because of the tax burden that would apply to an outright sale. In this way, like-kind exchanges are a powerful tool that accelerates domestic investment, and the provision is facilitating a faster and smoother transition to the post-pandemic economy.

**Like-kind exchanges contribute to financial stability.** Exchanges have helped offset the general, post-pandemic decline in commercial real estate activity associated with rising interest rates and maturing loans, work-from-home trends, and economic uncertainty. In the first half of 2023, overall commercial real estate transaction activity fell more than 22 percent below its pre-pandemic level in 2019 (Real Capital Analytics). At the same time, industry data suggests the number of like-kind exchanges initiated increased nearly 15 percent (Federation of Exchange Accommodators). This

sustained exchange activity in a weakened market has supported price stability and reduced the likelihood of a market shock. As noted by Marcus & Millichap, one of the largest commercial real estate brokerages, “the liquidity created by 1031 exchanges can reduce the risk of commercial property default, which in turn reduces risk in the banking and financial systems that would otherwise imperil the broader financial market.”

**Rules for like-kind exchanges are narrowly tailored and well-designed.** Congress first codified like-kind exchanges in 1921, not long after enactment of the income tax itself. Over time, Congress has thoughtfully modified and improved the provision. Since 1984, laws have eliminated potential abuses, created strict and uniform rules and procedures for an exchange, and tightened section 1031 to avoid unintended results. In 2017, Congress narrowed the provision to apply only to real property. Today, exchanges represent a large share of overall real estate transaction activity. Research by Professors David Ling (University of Florida) and Milena Petrova (Syracuse University) estimates that 10 to 20 percent of commercial real estate transactions involve a like-kind exchange.

**Like-kind exchanges help small and minority-owned businesses expand and grow.** Veteran-owned, women-owned, and minority-owned businesses were hit especially hard by the pandemic. These firms and other small businesses use like-kind exchanges to expand and build equity in their companies without having to rely on bank loans and other third-party lending that can be difficult to obtain. Small firms and entrepreneurs lack access to the deep capital markets that finance the activities of large corporations. Like-kind exchanges help small and minority-owned businesses grow organically, without overreliance on unsustainable levels of debt and leverage. Because owners are able to reinvest their proceeds on a tax-deferred basis, properties acquired in a like-kind exchange carry less overall debt—30 percent less than similar real estate acquired outside of a like-kind exchange.

**Like-kind exchanges are an engine of job creation.** Research by Ernst and Young (which was updated in 2022) reported that in 2021 economic activity generated by like-kind exchanges supported 976,000 jobs generating \$48.6 billion of labor income and contributing \$97.4 billion to the US GDP. Employment directly and indirectly supported by exchanges includes jobs for skilled tradesmen, architects, designers, building material suppliers, movers, building maintenance and cleaning staff, security, landscapers, qualified intermediaries, real estate brokers, title insurers, settlement agents, attorneys, accountants, lenders, property inspectors, appraisers, surveyors, insurers, and contractors.

According to Ernst and Young, this economic activity generated \$13.1 billion in federal, state and local tax revenue. They also found that like-kind exchanges produce an additional \$6 billion in federal tax revenue due to foregone depreciation (reduced deductions) on the replacement property. Since 1031 exchanges generate significantly more revenue than would result from capping the provision, any cap or change to section 1031 would be detrimental to both the public and private sectors of the U.S. economy. By encouraging the reinvestment of capital and stimulating property improvements, exchanges create a more dynamic, job-creating real estate market which benefits the entire US economy.

**Farmers, ranchers, and forest owners heavily rely on like-kind exchanges.** Farmers, ranchers, and forest owners use like-kind exchanges to combine acreage, acquire higher-grade land, mitigate environmental impacts, or otherwise improve the quality of their operations. They may use like-kind exchanges to reconfigure their businesses so that young or beginning farmers can join the

business. Retiring farmers are able to exchange their most valuable asset, their farm or ranch, for other real estate without diminishing the value of their life savings.

**Like-kind exchanges promote land conservation and environmental protection.** Land conservation organizations rely on like-kind exchanges to preserve open spaces for public use or environmental protection. Land conservation transactions often involve the exchange of environmentally sensitive areas for other less sensitive privately held property, which can be put into production. These transactions protect environmentally significant land and open space for the future while enabling private landowners to preserve capital for expansion or diversification of existing operations, retirement, or other needs.

**Increasing the supply of affordable rental housing requires like-kind exchanges.** Like-kind exchanges can fill gaps in the housing supply not covered by other incentives for the development of affordable housing. Multifamily housing transactions represent 40 percent of real estate like-kind exchanges. Expanding workforce housing will require significant investment of private capital. However, tax incentives like the low-income housing tax credit do not apply to land acquisition costs. Investors can use section 1031 to acquire land for the development of new housing. New limits on like-kind exchanges would increase the cost of rental housing. The Ling-Petrova study concluded that an owner would have to raise rents significantly on tenants to offset the tax consequences of repealing section 1031.

**States and localities depend on like-kind exchanges for tax revenue.** As stated above, like-kind exchanges generate much-needed tax revenue for States and localities. The more frequent turnover of real estate attributable to section 1031 generates property transfer taxes and recording fees, as well as property reassessments that increase the tax base. Most importantly, because of lower debt and greater capital investment rates, the taxes paid on the subsequent sale of these properties are significantly greater.

**For many Americans, like-kind exchanges are a principal tool for retirement savings.** The self-employed often own real estate as part of, or incidental to, a small business venture, such as a farm, restaurant, or service business. These individuals often lack a company-sponsored 401(k) plan, and reinvesting proceeds from the sale of actively managed real estate into institutionally managed, passive interests in real estate through a like-kind exchange may be their only form of retirement saving. Much like traditional pension and deferred contribution plans, these arrangements allow small business owners and the self-employed to generate long-term income and a secure retirement. Similarly, prudent portfolio management by institutionally managed real estate funds using like-kind exchanges provides important diversification in retirement savings options for workers investing through 401(k) plans.

**Like-kind exchanges reduce the cost of capital and make the economy more efficient.** Section 1031 expands opportunities for businesses to relocate to better, more productive locations. The provision increases taxpayers' ability to exchange older assets for newer assets better suited to the needs of surrounding communities and tenants. By eliminating the "lock-in" effect caused by taxing prior gain at the time of a transaction, exchanges lift the velocity of reinvestment—the rate at which businesses convert assets to better match their business needs, to operate more efficiently, or to generate more income. Taxpayers using a like-kind exchange acquire replacement property that is valued more than 15 percent higher on average than the relinquished property.

**Taxes are frequently collected in the year of the like-kind exchange.** The Ling-Petrova study found that in more than a third of exchanges, property owners pay some capital gains tax in the year of the exchange because of differences in the values of the replacement and relinquished property. In addition, the overwhelming majority of replacement properties acquired in a like-kind exchange are ultimately disposed of through fully taxable sales (not subsequent like-kind exchanges). The Ling-Petrova study also found that fewer than 20 percent of replacement properties are disposed of through a subsequent like-kind exchange.

**Lastly, the deferral of tax on gains reinvested in a business represents sound tax policy that is consistent with other provisions of the tax code.** The tax law has long treated most business entity formations, restructurings, and combinations as transactions that do not, and generally should not, give rise to the recognition of gain. *See, e.g.*, I.R.C. §§ 351, 721. This is true even though, unlike section 1031, they all involve a transfer of property, from one taxpayer to another, in exchange for property that is materially different in kind. These nonrecognition rules ensure that the built-in gain or loss (and other tax attributes) of the party benefiting from nonrecognition are preserved, for future taxation in the ordinary course, largely as if the transaction had not occurred.

\* \* \*

The benefits of section 1031 clearly were well-understood when the Senate voted unanimously in 2021 to amend its budget resolution to include an amendment in support of preserving like-kind exchanges. Today, following years of careful legislating and regulatory rulemaking, section 1031 supports job growth and stable commercial real estate markets; creates a ladder of economic opportunity for small businesses, cash-poor entrepreneurs, and farm, ranch, and forest owners; and constitutes an important tool for the environmental conservation of land for future generations. We encourage you to preserve this long-standing feature of the tax code and reject efforts to curtail it. If you or your staff would like additional information or have questions regarding like-kind exchanges, please do not hesitate to contact Ryan McCormick of The Real Estate Roundtable at (202) 639-8400 or [rmccormick@rer.org](mailto:rmccormick@rer.org).

Sincerely,

Alternative & Direct Investment Securities Association  
American Cotton Shippers Association  
American Farm Bureau Federation  
American Hotel and Lodging Association  
American Land Title Association  
American Resort Development Association  
American Seniors Housing Association  
American Society of Farm Managers and Rural Appraisers  
Asian American Hotel Owners Association  
Associated Builders and Contractors  
Associated General Contractors of America  
BOMA International  
CCIM Institute  
Commercial Real Estate Finance Council

Federation of Exchange Accommodators  
Forest Landowners Association  
ICSC  
Institute for Portfolio Alternatives  
Institute of Real Estate Management  
Land Trust Alliance  
Latino Hotel Association  
Manufactured Housing Institute  
Mortgage Bankers Association  
NAIOP, the Commercial Real Estate Development Association  
Nareit  
National Apartment Association  
National Association of Black Hotel Owners, Operators & Developers  
National Association of Home Builders  
NATIONAL ASSOCIATION OF REALTORS®  
National Cattlemen's Beef Association  
National Corn Growers Association  
National Multifamily Housing Council  
REALTORS® Land Institute  
The Conservation Fund  
The Nature Conservancy  
The Real Estate Roundtable