

Agriculture 1031 Exchanges



Harnessing the Power of Agriculture 1031 Exchanges

1031 Insight April 2023

1031 Exchanges permit taxpayers to defer the taxes that arise from the sale of investment or business real estate. An exchange is a powerful tool for those involved in agriculture such as farmers, corporate farm owners, ranchers, institutional investors, and individual investors. Structuring a transaction as a 1031 Exchange allows a taxpayer to reinvest 100% of the gains from the sale into new real estate opportunities by deferring taxes that could be up to 30% to 40% of the gain. The taxes that may be deferred include capital gains, state tax, net investment income tax (NIIT), Affordable Care Act tax, and, if applicable, depreciation recapture tax.

Properties that qualify for tax deferral include farms, ranches, raw land, and mixed-use property comprised of land with a primary residence. Interests in real property such as oil, gas, mineral rights, and water rights may also be exchanged.

We see taxpayers in the agriculture community utilizing 1031 Exchanges to improve and expand operations, to move into acreage more suitable for productive agricultural use, or to dispose of property/operations and transition into other Like-Kind eligible property such as apartments, industrial, or even passive investments.

Agriculture 1031 Exchanges include:

Farms, Ranches, Raw Land and Agricultural Land

Farms, ranches, raw land, and farmland are all eligible for 1031 tax deferral.

Mixed-Use Property

[Mixed-Use 1031 Exchanges](#) are used when a portion of the property qualifies as property held for use in a business or investment while the other portion is a primary residence. When selling a farm or ranch that includes a farm or ranch house, the personal residence can be separated from the total farm sales price, and the balance can be sold as property held for use in business or for investment. The personal residence may qualify for a \$250,000 single /\$500,000 married exclusion on the gain under Section 121 of the Internal Revenue Code (IRC), while the land portion including ranches, farms, raw and agricultural land would be subject to Section 1031.

Other Interests in Real Property

Certain interests in real property, such as oil, gas and mineral rights, water rights, easements and conservation easements, timberland and raw land, unharvested crops, fee interests wind turbines, and leasehold interests may be exchangeable for a fee interest in real property such as land, apartments, industrial, etc. The IRS generally looks to State law as a relevant factor in determining whether the interest in the property is treated as real property that qualifies for Section 1031 tax deferral or as personal property. Courts generally look to the underlying nature of the intangible property rights. If the right is perpetual, such as an easement or a royalty interest, it is generally real property for Section 1031 purposes. In states that treat water rights as real property interests, perpetual water rights are like-kind to a fee interest and may be exchanged for other real estate. [Click here for more information.](#)

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