

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 19014233
E. RICCIARDELLI)
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OPINION

Representing the Parties:

For Appellant: Scott B. Burkholder, Attorney

For Respondent: David Gemmingen, Tax Counsel IV

For Office of Tax Appeals: Mai C. Tran, Tax Counsel IV

E. S. EWING, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, E. Ricciardelli (appellant) appeals an action by respondent Franchise Tax Board (FTB) proposing \$59,257 of additional tax, and applicable interest, for the 2012 tax year.

Office of Tax Appeals Administrative Law Judges Elliott Scott Ewing, John O. Johnson, and Nguyen Dang, held an oral hearing for this matter in Cerritos, California, on February 19, 2020. At the conclusion of the hearing, the record was closed and this matter was submitted for decision.

ISSUE

Whether appellant timely identified replacement property to qualify for nonrecognition of gain treatment under Internal Revenue Code (IRC) section 1031.

FACTUAL FINDINGS

1. On April 30, 2012, appellant entered into a deferred exchange agreement with ANI X31, Inc. (ANI or qualified intermediary) to facilitate a like-kind exchange of appellant’s real property located on Crescent Heights Boulevard in West Hollywood, California (Crescent Heights property or relinquished property).

2. On May 21, 2012, ANI, as the qualified intermediary for the E. Ricciardelli Living Trust dated December 22, 2010 (Trust), sold the Crescent Heights property on behalf of appellant to an unspecified third party for \$1,500,000, as reflected on the Seller's Final Settlement Statement dated May 24, 2012. The escrow company, Sterling West Escrow, issued to appellant, as trustee of the Trust, a 2012 Form 1099-S, which reported gross proceeds of \$1,500,000 from the May 21, 2012 sale of the Crescent Heights property.
3. In a letter to appellant dated May 22, 2012, HSBC Bank confirmed that the account for appellant's mortgage on the Crescent Heights property was paid in full. Attached to the bank's May 22, 2012 letter is a loan activity schedule which shows that the principal of \$546,100.98 for the Crescent Heights property was paid in full on May 21, 2012.
4. On or about May 21, 2012, the escrow company wired appellant's net proceeds of \$944,999.59 to appellant's qualified intermediary, as reflected in a letter to appellant from Sterling West Escrow dated May 24, 2012.
5. On July 5, 2012, which was 45 days after appellant sold the Crescent Heights property on May 21, 2012, appellant signed a contract for the purchase of real property located on Topanga Canyon Boulevard in Woodland Hills, California (Topanga Canyon property). However, the escrow on appellant's purchase of the Topanga property never closed.
6. On July 8, 2012, appellant signed a "Designation Form," identifying the Topanga Canyon property and real property located on West Channel Road in Santa Monica, California (Channel Road property), as well as a third real property located on Hacienda Place in West Hollywood, California, as the replacement properties.¹ The receipt acknowledgment portion of the Designation Form is not signed or dated by ANI.
7. On November 16, 2012, which was 179 days after appellant sold the Crescent Heights property on May 21, 2012, appellant purchased the Channel Road property, which he claimed as replacement property for purposes of a like-kind exchange.
8. Appellant filed federal and California returns for the 2012 tax year and reported the like-kind exchange on a 2012 Internal Revenue Service (IRS) Form 8824, Like-Kind Exchanges. Appellant reported on Form 8824 that the relinquished property was acquired on July 20, 2004, and was "given up" on May 21, 2012. Appellant also reported on Form 8824 that the replacement property was identified by written notice to another

¹ Appellant signed the Designation Form as trustee of the Trust.

- party on May 21, 2012, and was acquired by appellant on November 16, 2012. Appellant indicated on Form 8824 that the replacement property was identified on May 21, 2012; however, the record shows that the actual date of the identification was July 8, 2012.
9. FTB audited appellant's 2012 California return.² At audit, FTB disallowed the reported like-kind exchange and determined that appellant realized a taxable gain of \$476,629 that should have been recognized for 2012 from the sale of the Crescent Heights property based on a sale price of \$1,500,000 less an aggregate adjusted basis and associated sales costs of \$1,023,371.³
 10. On January 17, 2017, FTB issued a Notice of Proposed Assessment (NPA), disallowing the like-kind exchange reported on appellant's Form 8824. The NPA indicates that FTB increased appellant's reported taxable income by the \$476,629, from \$586,424 to \$1,063,053, due to the disallowance of the reported like-kind exchange under R&TC section 18031, which conforms to IRC section 1031. As a result, the NPA proposed additional tax of \$59,257, plus interest.⁴
 11. After appellant protested the NPA, FTB issued a Notice of Action (NOA) dated December 7, 2018, affirming the NPA. The NOA states that the Channel Road property was not like-kind property because appellant did not timely identify the Channel Road property within the 45-day identification period required by IRC section 1031(a)(3)(A) and therefore the Crescent Heights property did not qualify for gain deferral treatment under IRC section 1031.
 12. Appellant then filed this timely appeal.

² At the oral hearing in this matter, appellant's counsel stated that the IRS did not audit appellant's return for the 2012 tax year.

³ FTB's calculation of the gain is detailed in the addendum attached to FTB's opening brief. Appellant has not questioned FTB's calculation of the gain of \$476,629.

⁴ FTB suspended interest for the time period provided by R&TC section 19116.

DISCUSSION

IRC section 1001 generally requires recognition of the entire amount of gain or loss on the sale or exchange of property.⁵ However, for the tax year at issue,⁶ IRC section 1031(a)(1) provides for the nonrecognition of such gain or loss on “the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.”⁷

IRC section 1031(a)(3) contains rules that govern the time-periods during which deferred like-kind exchanges must be completed for nonrecognition treatment. IRC section 1031(a)(3)(A) requires that the replacement property be identified within 45 days of the transfer of the relinquished property (identification period). In addition, IRC section 1031(a)(3)(B) requires that the replacement property be acquired within the earlier of: 1) 180 days of the transfer of the relinquished property; or 2) the filing due date (including extension) for the taxpayer’s tax return for the year wherein the taxpayer transferred the relinquished property (exchange period).

Unidentified property, however, may qualify as replacement property if it is received by the taxpayer before the end of the 45-day identification period. (Treas. Reg. § 1.1031(k)-1(c)(1).)⁸ Other than the exception provided by Treasury Regulation section 1.1031(k)-1(c)(1), any property received by the taxpayer that is identified outside the identification period or received outside the exchange period does not qualify as like-kind property. (IRC, § 1031(a)(3).) These requirements are mandatory for transfers of property made on or after June 10, 1991. (*Dobrich v. Commissioner*, T.C. Memo. 1997-477, affd. (1999) 188 F.3d 512 [nonpub. opn.].) The identification period begins on the date the taxpayer transfers the relinquished property and ends at midnight on the 45th day thereafter. (Treas. Reg. § 1.1031(k)-3(b)(2)(i).)

Treasury Regulation section 1.1031(k)-1(c)(2) provides that property is properly

⁵ California law conforms to IRC section 1001 under R&TC section 18031.

⁶ For the 2012 tax year, California conforms to the January 1, 2009 version of the IRC. (R&TC, § 17024.5(a)(1)(O).)

⁷ California law conforms to IRC section 1031 under R&TC section 18031.

⁸ In general, when applying the IRC for California personal income tax purposes, federal regulations (temporary or final) issued by “the secretary” shall be applicable as California regulations to the extent they do not conflict with the R&TC or regulations issued by FTB. (R&TC, § 17024.5(d).)

identified as replacement property only if the property is designated as replacement property in a written document signed by the taxpayer and hand delivered, mailed, telecopied, or otherwise sent before the end of the identification period to a specified person involved in the exchange, such as an intermediary. The replacement property received by the taxpayer will be treated as property that is not of a like kind to the relinquished property if the property received is not substantially the same property as identified. (Treas. Reg. § 1.1031(k)-1(d)(1)(ii).)

Appellant relinquished the Crescent Heights property on May 21, 2012. The identification period ended 45 days later on July 5, 2012. The Designation Form identifying the Channel Road property as a potential replacement property is signed by appellant on July 8, 2012, three days after the end of the 45-day identification period. Further, as appellant did not acquire the Channel Road property until November 16, 2012, the Channel Road property cannot qualify for the exception for unidentified property acquired within the 45-day identification period. (Treas. Reg. § 1.1031(k)-1(c)(1).) Therefore, appellant failed to identify the Channel Road property as replacement property within the statutory 45-day identification period.

Appellant argues that he timely designated the Topanga property as replacement property and completed a timely exchange when he acquired the Channel Road property. Appellant contends that he completed a valid exchange for like-kind property when he identified the Topanga property by entering into a contract to buy the Topanga property on July 5, 2012, or alternatively, that he substantially complied with the identification requirements by identifying the Channel Road property a mere three days after the 45-day identification period had expired. We disagree.

Because appellant never acquired the Topanga property, the Topanga property cannot be considered replacement property for the Crescent Heights property. Appellant cannot satisfy the identification requirements with a property that he did not ultimately purchase. (See Treas. Reg. § 1.1031(k)-1(d)(1)(ii) [replacement property received must be substantially the same property as identified].) Although appellant ultimately acquired the Channel Road property within the 180-day exchange period, he identified that property after the 45-day identification period passed. The replacement property identified within the identification period must be substantially the same property acquired within the exchange period. (Treas. Reg. § 1.1031(k)-1(d)(1)(ii).)

At the oral hearing in this matter, appellant’s representatives also argued that we should find an equitable reason for allowing the nonrecognition of gain. However, the plain language of the statute does not allow for good faith attempts to validate what is otherwise an exchange transaction that does not comply with the mandatory 45-day identification period. (IRC, § 1031(a)(3)(A) [“any property received by the taxpayer shall be treated as property which is not like-kind property if such property is not identified as property to be received in the exchange on or before the day which is 45 days after the date on which the taxpayer transfers the property relinquished in the exchange”].) As such, the Channel Road property is not like-kind property and appellant is not entitled to defer gain from the sale of the Crescent Heights property.

HOLDING

Appellant failed to timely identify replacement property for purposes of nonrecognition of gain pursuant to IRC section 1031.

DISPOSITION

FTB’s action is sustained.

DocuSigned by:
Elliott Scott Ewing
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Elliott Scott Ewing
Administrative Law Judge

We concur:

DocuSigned by:
John O Johnson
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John O. Johnson
Administrative Law Judge

DocuSigned by:
Nguyen Dang
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Nguyen Dang
Administrative Law Judge

Date Issued: 5/27/2020