

**Nominee for a Key Treasury Post Tells Senate Panel that IRS Plans to Issue Guidance that Should Address Tax Consequences to Taxpayers Who Were Unable to Complete an Exchange Due to a QI failure**

A nominee for a high level tax policy position in the Treasury Department stated in his confirmation hearings earlier this month that the IRS plans to issue guidance addressing the status of accounts held by qualified intermediaries. Assistant Treasury Secretary for Tax Policy Nominee Michael Mundaca told Senate Finance Chairman Max Baucus that, “the published guidance should address the tax consequences to taxpayers who lost money or property, or who were unable to complete an exchange, due to a QI failure.” Mr Mundaca did not, however, give any indication of exactly what the guidance would say or when the IRS would issue the guidance.

Senator Baucus' question and Mr. Mundaca's answer on this issue are set forth in full below:

**QUESTION FROM SENATOR BAUCUS TO MR. MICHAEL MUNDACA:**

There has been some concern on the part of Congress about a few recent high profile bankruptcies by qualified intermediaries in IRC section 1031 transactions leading to defalcations and failed IRC section 1031 transactions when funds held by qualified intermediaries were not available to purchase the replacement property. This result causes taxpayers hardship resulting from taxation on gains on income that has disappeared. I understand that the IRS has plans to issue guidance on this matter. Specifically, in the 2008-2009 Priority Guidance Plan or ‘Business Plan’ the IRS included a reference to “[g]uidance under §1031 regarding the treatment of accounts held jointly by the taxpayer and a qualified intermediary.”

As you know, the IRS can issue rules or regulations covering the requirements for qualified intermediaries under IRC section 1031. Most regulatory guidance by the IRS falls under the General Counsel's general responsibilities. Can you update the Committee on the guidance on this issue and whether the IRS will issue rules to help better ensure that taxpayers' funds held by qualified intermediaries are available when the replacement property is scheduled to close?

**ANSWER BY MR. MICHAEL MUNDACA TO SENATOR BAUCUS:**

Treasury and the IRS are aware that the failures of several large qualified intermediaries (QIs) have resulted in taxpayers who initiated a section 1031 transaction being unable to complete an exchange because the QI filed for bankruptcy or defaulted on its obligations. As you note, the 2008-2009 Priority Guidance Plan includes a project to address the status of accounts held by QIs. The published guidance should address the tax consequences to taxpayers who lost money or property, or who were unable to complete an exchange, due to a QI failure. In general, a taxpayer considering a section 1031

exchange transaction is free to determine whether to utilize the services of a QI, and if so, to negotiate with the QI regarding how the taxpayer's funds – including proceeds from the sale of relinquished property – are held by the QI pending completion of the exchange. For example, a taxpayer and a QI may agree that sale proceeds of relinquished property must be placed in a trust or escrow account. Section 1031 and the regulations thereunder do not prescribe any particular arrangement or requirement regarding how funds are held.