

# The 1031 Like-Kind Exchange Is a Key Tool for Investing in Diverse and Inclusive Communities

By Dan Wagner, Senior Vice President Government Relations The Inland Real Estate Group

As property owners strive to put diversity and inclusion concepts into action, the like-kind exchange established in Section 1031 of the U.S. tax code can serve as a powerful tool that fosters economic development and promotes job growth for people from all walks of life.

For 100 years, the like-kind exchange has allowed real estate owners to exchange their property for other income-producing properties and defer the tax on any unrealized gain. When the owner eventually liquidates the investment, the government collects the full amount of taxes. In many cases, the new property grows in value beyond the original investment, thus yielding an even greater value for property owners and increased tax revenue for the government.

Section 1031 can benefit a variety of people in various socio-economic and demographic groups. It is the ultimate equal opportunity tax code provision because it provides an efficient and effective means for individuals to grow their wealth. More importantly, it also assists and incentivizes large economic impact commercial real estate projects in underserved markets that can have a positive effect on low-income, minority, and inner-city neighborhoods.

## Investment in Underserved Communities

Recently, the Biden Administration introduced a proposal to cap the amount of 1031 like-kind exchange real estate at just \$500,000. Unfortunately, this cap would have a materially negative impact within the communities that his American Families Plan and infrastructure plans are intending to help. By allowing property owners to defer capital gains taxes without a threshold limit, the like-kind exchange encourages and channels those dollars into real estate in underserved areas. For instance, the additional capital saved by not having to pay the tax immediately can be invested to help reposition an abandoned shopping area or an underused warehouse. These outdated properties can be transformed into more productive uses, such as affordable work-force housing or a job-generating e-commerce hub. In fact, the independent Ling and Petrova study confirmed that property owners who leveraged the like-kind exchange garnered appreciably greater capital investment in properties compared to those who purchased without an exchange.

But don't just take my word for it. Here are just a few poignant testimonials that support this position:

"As the Black community explores avenues for growth of their financial opportunities...the 1031 like-kind exchange (as it is) is more important now than ever," said Norman Alexander, President of the Ridgecrest Area REALTOR® Association and a member of the California Association of Black Real Estate Professionals.

"Every time we sell an apartment complex, we use the 1031; and if it were not available, we would not be able to make that transaction," said Bill Brown, 2017 Past President of the National Association of REALTORS® who is an African American business owner of Springhill Real Estate Partners. Brown further stated, "My Company spends anywhere from \$7,000 to \$10,000 per unit on remodeling. This helps provide jobs for laborers as well as materials such as carpeting, cabinets and many other goods." This continuous remodeling not only provides jobs in the community, but it also improves the quality of life for those who rent and live in these apartments.

David Doig, President and CEO of Neighborhood Initiatives developed a national grocery store in the food desert of a Chicago's Southside Bronzeville neighborhood. The site was formerly the demolished Ida B. Wells Public Housing Complex where it remained a vacant lot for more than 15 years. David's company developed a Mariano's grocery store in its place and then a New York investment group purchased the new development through a 1031 like-kind exchange. This outside capital infused a rebirth of jobs, housing, and commerce into the community.



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“We need to keep the 1031 like-kind exchange (as it is) in our tax code because it is another tool to encourage private capital to flow into commercial real estate projects that will help revitalize our underserved communities,” said Leon Walker, President and CEO of DL3 Realty and developer of the Wholefoods, Starbucks and Chipotle in Chicago’s Southside Englewood Community.

## Investment in Job Creation

Jobs. Jobs. Jobs. Everyone on both sides of the political spectrum agrees that a robust job market is important for creating pathways to growth in underserved communities. It is a proven fact that like-kind exchanges have a multiplier effect in a community when it comes to creating and maintaining jobs. An Ernst and Young (E&Y) study concluded that if Section 1031 is limited or eliminated, real estate transactions would decrease, the cost of capital would increase, and GDP would contract. The study found that 1031 exchanges generate \$4.4 billion in additional investment and 568,000 jobs each year. This equates to labor income of \$27.5 billion during 2021. A majority of these jobs come from the capital improvements that are made to properties after a like-kind exchange which create jobs including: electricians, carpenters, plumbers, contractors, masons, and building material suppliers.

An important part of our economy are the trade unions that provide a strong and talented workforce. “Our local IBEW 701 is very involved with economic development and the 1031 like-kind exchange is a great tool to create jobs for our members,” said Frank Furco, Business Manager of IBEW Local 701.

## Investment in Pension Income for IBEW Local 701 Union Members and More

The International Brotherhood of Electrical Workers Local 701 supports the 1031 like-kind exchange because Section 1031 transactions are important to Real Estate Investment Trusts (REITs) (and therefore the pensions and 401 (k) plans that invest in REITs). Specifically, Section 1031 enables a REIT to effectively manage its real estate portfolio, exchanging properties to manage risk and maximize return. This benefits both working and retired Americans that own REIT stocks in their retirement savings funds, especially trade unions who fund their own pensions. For example, IBEW 701 invests in REITs for their members’ pension funds which provides a strong case to ensure REITs remain strong. Many of these members work and live in the very same communities that benefit from the economic expansion provided by the 1031 like-kind exchange.

## 1031 Like-Kind Exchanges Generate Tax Revenue

From a policy perspective, it is also important to note that capping the 1031 like-kind exchanges could also reduce taxable income to the government. The E&Y Study highlights that tax revenue to federal, state and local governments related to 1031 transactions totals over \$7 billion a year. Income and sales tax revenues from jobs and economic activity generated through exchanges would decline significantly if Section 1031 were limited.

## Conclusion

It is imperative to help economically underserved and disadvantaged populations. While reasonable minds can debate specifics, it is also important not to do harm to the very same communities we seek to help. A practical and tangible way to help provide opportunities for people from a variety of backgrounds and economic status is through supporting the Section 1031 like-kind exchange and not capping its ability to help transform communities for the better. It is crucial that our elected officials know how essential this tax code provision is to providing opportunities to their constituents in the communities they represent. **Please go to [www.ipa.com/1031s/](http://www.ipa.com/1031s/) to learn how you can help preserve this vital tool of economic security.**

