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Like-Kind Exchanges and Involuntary Conversions (Related Articles)

BROAD SCOPE OF SECTION 470 CATCHES MANY NON-ABUSIVE TRANSACTIONS

BY RICHARD M. LIPTON

Once again, Congress seems to have employed an elephant gun to kill a tax shelter. New Section 470 goes way beyond the abusive SILO transactions that were its intended target and will affect a significant percentage of real estate partnerships. Not only are taxable partners subjected to loss disallowance, but the partnerships will face an enormous compliance burden of determining if any tax-exempt entities have an ownership interest through all tiers of owners.

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As part of the American Jobs Creation Act of 2004 (AJCA), P.L. 108-357, 10/22/04, Congress enacted new Section 470, which places a limitation on deductions allocable to property used by governmental or other tax-exempt entities. This provision was enacted to address "sale-in, lease-out" (SILO) transactions that were used to shift the tax benefits with respect to depreciable property from nontaxable persons to taxable parties that could use the tax benefits.

Although arguments could be made that not all SILO transactions were abusive,[1] it certainly was within Congress's purview to limit the losses that are available from such transactions. Congress, however, went much further. New Section 470 affects many routine transactions in which a partnership containing both taxable and tax-exempt persons owns rental real property. This common form of ownership is generally not abusive, and any potential tax benefits to the taxable person are usually addressed through reliance on a partnership agreement that complies with the strict allocation rules in Section 514(c)(9)(E).

Section 470 does not draw any fine distinctions, however, and it will adversely affect most partnerships that have both taxable and tax-exempt partners. As will be discussed in more detail below, the operation of the new provision "punishes" the taxable partners for entering into a partnership with tax-exempt partners by potentially disallowing losses. And, in addition to this severe economic impact, there will be a substantial compliance burden as every real estate partnership will have to inquire, all the way up the chains of ownership, if any partner is a tax-exempt entity.

THE DEPRECIATION DEDUCTION

A taxpayer is allowed to recover, through annual depreciation deductions, the cost of certain property used in a trade or business. In general, a taxpayer is treated as the tax owner of (and is entitled to depreciate) property leased to another party if the taxpayer acquires and retains significant and genuine attributes of a traditional owner of the property, including the benefits of appreciation and the risk of loss. No single factor is determinative of whether a lessor will be treated as the owner of property. Rather, the determination is based on all of the facts and circumstances.

In *Frank Lyon Co.*, 435 U.S. 561, 41 AFTR2d 78-1142 (1978), the Supreme Court was faced with the issue of whether a sale-leaseback transaction should be respected for federal income tax purposes. The Court found the arrangement would be respected if "there is a genuine multiple-party transaction with economic substance that is compelled or encouraged by business or regulatory realities, is imbued with tax-independent considerations, and is not shaped solely by tax-avoidance features to which meaningless labels are attached."

Tax-exempt use property. Under pre-AJCA law, "tax-exempt use property" had to be depreciated on a straight-line basis over a recovery period equal to the longer of the property's class life or 125% of the lease term. The purpose of these rules was to prevent the transfer of accelerated depreciation with respect to tax-exempt use property to taxable persons.

Tax-exempt use property was defined as tangible property leased (other than a short-term lease) to a tax-exempt entity. Such an entity included not only organizations described in Section 401 and 501 but also all governmental organizations and foreign persons (even if the foreign persons were subject to taxation in other jurisdictions). Tax-exempt use property did not include property that was used by a taxpayer to provide a service to a tax-exempt entity, and there were several other exceptions as well.

The AJCA changes. Congress was concerned, first, that some taxpayers were attempting to circumvent this policy through the creative use of service contracts with tax-exempt entities. Moreover, Congress believed that ongoing leasing activities between taxable persons and tax-exempt and governmental entities showed that the restrictions in prior law were not sufficient. Congress wanted to limit the ways in which the tax benefits inherent in leasing could be restricted in the case of property used by a tax-exempt or governmental entity.[2] That is, Congress did not want taxable entities to obtain the tax benefits from ownership of property if the property was leased to a tax-exempt entity except in certain situations. This was viewed as particularly a problem with respect to technological equipment.

To achieve this result, the AJCA contains four provisions concerning tax-exempt leasing, only one of which—new Section 470—is the focus of this article. The other three changes include:

1. The recovery period for qualified technological equipment and computer software leased to a tax-exempt entity (now defined to include domestic and foreign governments as well as foreign persons not subject to U.S. taxation) is increased to the longer of the property's assigned class life or 125% of the lease term.[3]

2. In determining the length of the lease term for purposes of the 125% calculation, the AJCA provides that the lease term includes all service contracts and other similar arrangements that follow a lease of property to a tax-exempt entity and that are part of the same transaction or series of transactions. Service contracts include any arrangements by which services are provided using property in exchange for fees that provide a source of repayment of the capital investment in the property.[4]

3. The AJCA did not eliminate the exception for short-term leases, but provides that for purposes of determining whether a lease of qualified technological equipment to a tax-exempt entity satisfies the five-year exception, the term of the lease does not include an option to renew or extend the lease if the rents under the renewal or extension are based on FMV determined at the time of the renewal or extension. The aggregate period of such renewals or extensions cannot exceed 24 months.[5]

SECTION 470

The AJCA expands the "passive loss" approach in Section 469 to tax-exempt use losses. Specifically, under Section 470(a), a taxable entity is not permitted to deduct any loss from tax-exempt use property in excess of the taxpayer's gross income from the lease for that tax year.[6]

Section 470 does not draw any fine distinctions, and will adversely affect most partnerships that have both taxable and tax-exempt partners.

Under Section 470(b), any tax-exempt use loss with respect to any tax-exempt use property is treated as a deduction with respect to such property in the next tax year. A taxable partner is entitled to the benefits of a tax-exempt use loss when the taxpayer disposes of its entire interest in the tax-exempt use property (under rules similar to those in Section 469(g)).[7] Thus, if a partnership has any tax-exempt use property, the portion of any loss that is a tax-exempt use loss generally will not be deductible by a taxable partner until the property is sold. This provision applies to all leases of tax-exempt use property entered into after 3/12/04.

Definitions

The most important aspects of Section 470 are the definitions of a "tax-exempt use loss" and "tax-exempt use property."

Under Section 470(c)(1), a tax-exempt use loss is the amount by which the sum of the aggregate deductions (other than interest) directly allocable to a tax-exempt use property, plus the aggregate deductions for interest properly allocable to such property, exceed the aggregate income from such property. Section 470(g)(2) expressly authorizes Regulations to provide for the allocation of interest expense for purposes of this provision.

"Tax-exempt use property" is gen-

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1 A SILO is simply a form of a sale-leaseback transaction, which is an extremely common transaction involving taxable persons. The difference in a SILO is that the seller-lessee is a tax-exempt entity that likely would not receive any benefit from the tax deductions related to the property that was conveyed. Although limitations on such benefits are already imposed by other provisions in the Code, such as Section 168(h), Congress attempted to obtain an overall limitation on tax benefits through new Section 470.

2 In a typical SILO transaction, a municipal transit authority would sell subway cars to taxable entities, which would then lease the cars back to the transit authority. The transit authority would continue to use the cars, and it would receive fees for entering into the transaction.

3 Section 168(g)(3)(A).

4 Section 168(i)(3).

5 Section 168(h)(3). The exception for short-term leases also does not apply to any period following the failure of a tax-exempt lessee to exercise a purchase option if the result of such failure is that the lease renews automatically at FMV rents.

6 Exceptions are provided for transactions with respect to which the low-income housing credit or the rehabilitation credit is allowable. These leases are beyond the scope of this article.

7 Section 470(e)(2).

erally defined for purposes of Section 470 by reference to Section 168(h). Section 168(h)(1)(A) provides that tax-exempt use property means that portion of any tangible property (other than nonresidential real property) leased to a tax-exempt entity.

The portion of any loss that is a tax-exempt use loss generally will not be deductible by a taxable partner until the property is sold.

With respect to nonresidential real property, Section 168(h)(1)(B)(i) provides that tax-exempt use property means the portion of the property leased to a tax-exempt entity in a "disqualified lease." A disqualified lease is defined in Section 168(h)(1)(B)(ii) as any lease of the property to a tax-exempt entity, but only if any of the following four conditions is met:

1. Part or all of the property was financed (directly or indirectly) by tax-exempt debt.
2. Under such lease there is a fixed or determinable purchase or sale option.
3. The lease has a term in excess of 20 years.
4. There is a sale-leaseback with respect to the property.

Under Section 168(h)(1)(B)(iii), however, nonresidential real property is not treated as tax-exempt use property unless more than 35% of the property is leased to tax-exempt entities. There are several exceptions in Section 168(h)(1), including one for property used in an unrelated trade or business of the tax-exempt entity.

Although Section 470 generally defines tax-exempt use property by reference to Section 168(h), it contains several important changes:

- The exceptions in Section 168(h) for short-term leases and leases of high-technology equipment are wholly inapplicable for purposes of Section 470.[8]
- For purposes of applying Section 470, any Section 197 intangible, or any property described in Section 167(f)(1)(B) (computer software) or (f)(2) (intangible assets that are separately acquired), is treated as if it were tangible property, so that the use of such property by a tax-exempt entity could give rise to a lease.[9]
- Section 470 does not apply to property that would be subject to a low-income housing or rehabilitation credit if such property were treated as tax-exempt use property solely because the property is owned by a partnership that has tax-exempt partners.[10]

Qualified allocations. The potentially severe impact of the cross-reference to Section 168(h) in the definition of tax-exempt use property in Section 470 arises because of Section 168(h)(6)(A). Under that section, if (1) any property that otherwise would not be tax-exempt use property is owned by a partnership which has both a tax-exempt entity and a person who is not a tax-exempt entity as partners, and (2) any allocation to the tax-exempt entity of partnership items is not a "qualified allocation," an amount equal to such tax-exempt entity's proportionate share of such property is treated as tax-exempt use property.

Section 168(h)(6)(B) provides that a qualified allocation is any allocation to a tax-exempt entity that has substantial economic effect and is consistent with such entity's being allocated the same distributive share of each item of income, gain, loss, deduction, credit, and basis, and such share remains the same during the entire period the entity is a partner in the partnership. Under Section 168(h)(6)(C), the proportionate share of the tax-exempt entity is such entity's largest proportionate share of income or gain of the partnership (excluding gain allocated under Section 704(c)), and if allocations vary during the period in which the tax-exempt entity is a partner, only the highest share is taken into account. Similar rules apply to any pass-through entity other than a partnership and to tiered partnerships.

What is so troubling about this rule is that a "qualified allocation" requires a pro rata allocation that never varies. A preferred return, incentive allocations, or any type of carried interest would not be consistent with a "qualified allocation." Thus, if a taxable entity and a tax-exempt form a partnership to develop real property, and the tax-exempt entity is to receive a preferred return on the money it invested, there would not be a "qualified allocation" even if the allocations in the partnership agreement fully satisfied the "fractions rule" of Section 514(c)(9)(E).[11]

The same result would occur if the developer put in 10% of the cash but was entitled to 20% of the profits after all cash contributions had received a stated return. In other words, even if the income allocated to the tax-exempt entity is not treated as unrelated business taxable income (UBTI), the underlying allocations would not be "qualified" for purposes of Section 168(h). Very few partnerships that own or develop real estate will have "qualified allocations."

To make matters worse, Section 168(h) is not limited in its scope to property held by partnerships and entities taxable as partnerships. Any "tax-exempt controlled entity," as defined in Section 168(h)(6)(F)(iii), also is treated as a tax-exempt entity. A tax-exempt controlled entity is any corporation if 50% or more (in value) of the stock on such corporation is held by one or more tax-exempt entities (other than a foreign person or entity). For example, a private REIT that is largely owned by 15 tax-exempt entities would be treated as a tax-exempt controlled entity. Where stock is publicly traded on an established securities market, stock held by a tax-exempt entity is not taken into account unless

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8 Section 470(c)(2)(A).

9 Section 470(c)(2)(B).

10 Section 470(c)(2), flush language.

11 Under Section 514(c)(9)(E), a partnership that owns debt-financed property must have allocations that (1) cannot result in a qualified organization's having a share of overall partnership income for any tax year greater than such partner's share of the overall partnership loss for the tax year for which such partner's loss share will be the smallest, and (2) have substantial economic effect under Section 704(b)(2). A qualified organization is generally any pension plan or any educational institution.

such entity holds at least 5% (in value) of the stock. A tax-exempt controlled entity can elect out of Section 168(h)(6)(F), but only if the tax-exempt entity agrees to treat any gain on any disposition of an interest in such entity as UBTI.

Exception

There is an important exception in Section 470(d) for certain leases (exempt leases) that meet certain stringent requirements:

1—Allowable amount. The tax-exempt lessee may not have more than an "allowable amount" of funds subject to either (a) any arrangement described in Section 470(d)(1)(B) or (b) any arrangement under which a reasonable person would conclude, based on the facts and circumstances, that funds were set aside or expected to be set aside.

Section 470(d)(1)(B) refers to a defeasance arrangement, a loan by the lessee to the lessor or any lender, a deposit arrangement, a letter of credit collateralized with cash or cash equivalents, a payment undertaking agreement, prepaid rent, a sinking fund arrangement, a guaranteed investment contract, financial guarantee insurance, and any similar arrangement.

An "allowable amount" of funds is generally equal to 20% of the lessor's adjusted basis in the property at the time the lease is entered into, although a higher percentage could be allowed by Regulations.[12] If the lessee has the option to purchase property for a fixed price or for other than the FMV of the property (determined at the time of exercise), the allowable amount at the time such option may be exercised may not exceed 50% of the price at which such option may be exercised.[13]

What is so troubling is that a 'qualified allocation' requires a pro rata allocation that never varies.

2—Equity investment. The taxpayer must make and maintain a substantial equity investment in the leased property. For this purpose, the taxpayer generally does not make or maintain a substantial equity investment unless (a) at the time the lease is entered into, the taxpayer initially makes an unconditional at-risk equity investment in the property of at least 20% of the taxpayer's adjusted basis in the leased property at that time, and (b) the taxpayer maintains such equity investment throughout the lease term.[14]

3—FMV. At all times during the lease term, the FMV of the property at the end of the lease term is reasonably expected to equal at least 20% of its initial value.[15]

4—Lessee's share of loss. There is no arrangement under which the lessee bears (a) any portion of the loss that would occur if the FMV of the leased property were 25% less than its reasonably expected FMV at the time the lease is terminated, or (b) more than 50% of the loss that would occur if the FMV of the leased property at the time the lease is terminated were zero.[16]

5—Purchase option. If the property has a class life of more than seven years (other than fixed-wing aircraft) and if the lessee has the option to purchase the property, the purchase price must equal the FMV of the property at the time of exercise of the purchase option.

Special Rules

Several special rules under Section 470 further broaden its potential impact.

1. Sections 1031(a) and 1033(a) will not apply if the exchanged or converted property is tax-exempt use property subject to a lease that was entered into before 3/13/04, and which would not have met the requirements for an exempt lease under Section 470(d) had such requirements been in effect.[17]

2. Sections 1031(a) and 1033(a) will not apply to an exchange if the replacement property is tax-exempt use property subject to a lease that is not an exempt lease under Section 470(d).[18] Thus, every acquiror of leased replacement property will need to determine whether there is any tax-exempt user of the property and, if there is, verify that the lease satisfies the requirements of Section 470(d).

3. If property was formerly tax-exempt use property, any deduction with respect to such property for any tax year will be allowed only to the extent of any net income from such property for that tax year.[19]

To make matters worse, Section 168(h) is not limited to property held by partnerships—any 'tax-exempt controlled entity' is treated as a tax-exempt entity.

In addition, the limitation on losses from tax-exempt use property is applied before the limitation under Section 469.[20] Section 470(g) provides the IRS with broad regulatory authority to carry out the purposes of Section 470.

As noted at the beginning of this article, one of the more interesting aspects of the interaction between Section 470 and Section 168(h)(6) is that the adverse impact is imposed on the taxable entities. Specifically, Section 470 disallows the tax-exempt use portion of the loss that otherwise would be allowed to the taxable partners.

For example, if a partnership is owned 40% by taxable partners and

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12 Section 470(d)(1)(C)(i). This amount is reduced to zero with respect to any arrangement that involves (1) a loan from the lessee to the lessor or a lender, (2) any deposit received, letter of credit issued, or payment undertaking entered into by a lender otherwise involved in the transaction, or (3) in a transaction that involves a lender, any credit support made available to the lessor in which any such lender does not have a claim that is senior to the lessor.

13 Section 470(d)(1)(C)(iii).

14 This requirement does not apply to leases with a term of five years or less.

15 Section 470(d)(2)(A)(ii).

16 Section 470(d)(3). The IRS is granted authority to issue Regulations under which this requirement is not met if the lessee bears more than a minimal risk of loss.

17 Section 420(e)(4)(A)(i).

18 Section 470(e)(4)(A)(ii).

19 This is similar to the rule for former passive activities under Section 469(f).

20 Section 470(e)(3).

60% by tax-exempt partners, its tax-exempt use portion would be 60% (i.e., the portion of its income and loss that is allocated to tax-exempt partners). Assuming that the partnership generates a loss and Section 470 applies, the taxable partners would not be entitled to deduct 60% of the loss that otherwise would be allocated to them, while there would be no adverse impact on the tax-exempt partners. Thus, the taxable partners will be "punished" for having entered into a partnership with tax-exempt partners unless the partnership agreement contains qualified allocations.

THE PROBLEMS RAISED BY SECTION 470

Section 470 has been criticized not because of its impact on the transactions at which it was targeted—the SILOs that Congress and the IRS believed to be abusive—but because of its unanticipated impact on "innocent" transactions in which property is not leased to a tax-exempt entity. These problems arise because of the employment of Section 168(h)—and particularly Section 168(h)(6)—in the definition of tax-exempt use property in Section 470. The exception in Section 470(d), although helpful, will not apply to many routine transactions.

Every acquiror of leased replacement property will need to determine whether there is any tax-exempt user and, if so, verify that the lease satisfies Section 470(d).

For example, many real estate partnerships or funds will have both taxable and tax-exempt partners. In a typical real estate partnership, the "equity" partners, which frequently will include tax-exempt entities, will be entitled to receive a return on (and frequently a return of) their equity before the "developer partner" receives any allocation of income. The developer partner has what is commonly referred to as a "carried interest" or a "promote," meaning that the developer partner will share in the income from the real property only if the development is successful.

Congress and the IRS long have been aware of these arrangements, and the Regulations under Section 514(c)(9)(E) place limits on how the partners can structure their economic arrangements without generating UBTI for the tax-exempt partners. Allocations that satisfy the requirements of Section 514(c)(9)(E) would not be "qualified allocations" within the meaning of Section 168(h)(6), however, because any type of a "promote" or "carry" is inconsistent with all partners being allocated the same share of all items of partnership income, gain, loss, or deductions for all periods. Thus, although most real estate partnerships will satisfy the requirements of Section 514(c)(9)(E), very few contain qualified allocations within the meaning of Section 168(h)(6).

The problems posed by Section 470 are not limited, however, to partnerships in which a developer and a tax-exempt entity join together to develop property. Problems also will arise in the case of tiered partnerships and other pass-through entities. For example, many hedge funds and other investment partnerships will invest a portion of their funds in real estate ventures. The partnership that is developing the real estate will know only that partnership XYZ is a partner in the partnership; it will not know whether any tax-exempt entities are partners in XYZ. Section 470 would require the lower-tier partnership to determine the percentage of XYZ that is tax-exempt entities in order to apply the limitation in Section 470. This is particularly a problem for a "fund of funds" and other tiered investment vehicles.

Moreover, the potential impact of Section 470 is not limited to tiered investments involving partnerships. A significant portion of the equity raised for real estate investments comes from REITs. The use of REITs as an investment vehicle has grown substantially as a result of the liberalization of the REIT rules over the past decade.

Furthermore, as long as a pension plan does not own more than 10% by value of the interests in any pension-held REIT within the meaning of Section 856(h)(3)(D),[21] the dividends received by a tax-exempt entity from the REIT will not be UBTI. As a result, many tax-exempt entities now use REITs as their vehicle of choice for making real estate investments. In other situations, a tax-exempt entity will interpose a C corporation (a "blocker corporation") between itself and the real estate partnership so as to prevent UBTI.

Nevertheless, it is possible for a REIT or a blocker corporation to be a tax-exempt controlled entity within the meaning of Section 168(h)(6)(F). This rule applies if 50% or more of the stock of the corporation is owned directly or indirectly by one or more tax-exempt entities. Moreover, the stock could be owned through a tiered own-

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21 A REIT is treated as a pension-held REIT if (1) at least one pension plan holds more than 25% (by value) of the interests in the REIT, or (2) one or more pension plans (each of which own more than 10% by value of the interests in such REIT) hold in the aggregate more than 50% (by value) of the interests in the REIT.

Practice Notes

What is so troubling about Section 470 is that a "qualified allocation" requires a pro rata allocation that never varies. A preferred return, incentive allocations, or any type of carried interest would not be consistent with a "qualified allocation." Thus, if a taxable entity and a tax-exempt form a partnership to develop real property, and the tax-exempt entity is to receive a preferred return on the money it invested, there would not be a "qualified allocation" even if the allocations in the partnership agreement fully satisfied the "fractions rule" of Section 514(c)(9)(E).

The same result would occur if the developer put in 10% of the cash but was entitled to 20% of the profits after all cash contributions had received a stated return. In other words, even if the income allocated to the tax-exempt entity is not treated as unrelated business taxable income (UBTI), the underlying allocations would not be "qualified" for purposes of Section 168(h). Very few partnerships that own or develop real estate will have "qualified allocations."

ership structure (such as through a hedge fund or other partnership that invests in a REIT), so that the REIT or a blocker corporation may not know whether it is a tax-exempt entity for purposes of Section 168(h)(6)(F). Thus, the presence of a REIT or a blocker corporation as an investor in a real estate partnership could have an adverse impact on the taxable partners in that partnership if the REIT or blocker corporation is treated as a tax-exempt controlled entity—a question that it is likely that no one ever considered.

What is even more odd about the treatment of REITs in this context is that again the "penalty" is imposed on the taxable investors and not the REIT that has tax-exempt investors.

EXAMPLE: A REIT is a tax-exempt controlled entity because exactly 50% of its investors are tax-exempt entities. The REIT, in turn, owns 60% (and taxable persons own 40%) of a partnership that owns rental property and which generates a loss of $1 million. As a result, 60% of the loss that is allocable to the taxable partners will be disallowed under Section 470. No portion of the loss allocable to the REIT will be disallowed, however, because the REIT is treated as a tax-exempt entity, which means that the taxable persons who invested through the REIT still will receive a tax benefit from the loss generated with respect to the real estate.

The potential disallowance of losses is the economic impact of Section 470. The more difficult problem may be compliance. In order to determine the amount of its tax-exempt use property, every partnership that owns real property will have to determine whether any of the partners are tax-exempt entities. If any of the partners are a partnership, the property-owning partnership will need to look through all of the "tiers" to determine the percentage of its owners that are, directly or indirectly, tax-exempt persons. Moreover, even if a partner is not a pass-through entity, the partnership would need to determine whether an entity is a tax-exempt controlled entity, meaning that an inquiry would need to be made as to the identity of the shareholders of every corporate partner. The difficulty in applying these rules is one of the reasons that the Service issued Notice 2005-29, 2005-13 IRB 796. Most property held by partnerships that have tax-exempt partners is effectively exempted by the Notice from the impact of Section 470 for pre-2005 tax years.

CONCLUSION

Section 470 will have an adverse impact on every partnership that could incur a loss and that has both taxable and tax-exempt partners. This is particularly a burden in the real estate industry, because rental properties often generate losses for a number of years, and a significant portion of the rental real estate in the U.S. is owned by partnerships that include taxable persons and tax-exempt entities (particularly charitable foundations and pension plans). Moreover, in most situations the tax-exempt entity will want to receive a preferential return on its investment, which will result in allocations that are not "qualified" for purposes of Section 168(h).

Most real estate partnerships will satisfy 514(c)(9)(E), but very few contain qualified allocations within the meaning of 168(h)(6).

It is hoped that Congress will recognize Section 470 cuts too wide a swath, and the scope of the legislation will be narrowed. Several possible approaches would achieve this goal, including legislation that would more narrowly confine a SILO transaction to situations in which the tax-exempt user controls the leased assets. Another approach, to the extent that Congress comes to see the cross-reference to Section 168(h)(6) as the problem, would remove from the scope of Section 470 any partnership that complies with the fractions rule in Section 514(c)(9).

The first approach has the benefit of keeping the scope of Section 470 consistent with its purpose, while the latter has the benefit of coordinating the applicable statutory provisions and rewarding those partnerships that have debt-financed property and that have taken the steps necessary to avoid UBTI. On the other hand, such an approach would not address partnerships that do not have debt financing or that were willing to accept UBTI.

For most practitioners, Section 470 will be a classic "unknown hazard" that could result in the disallowance of losses or that could make taxable an exchange of like-kind property. Although "administrative grace" lessened the potential broad impact of Section 470 in 2004, the provision is now in effect, and every tax practitioner needs to be aware of its broad scope. ■