INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

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District Director

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No.:
Years Involved:
Date of Conference:

LEGEND:

Taxpayer
X
Y
Z
Date 1
Date 2
A
B
C
D
City P
City Q
City R
City S
$h
$i
$j
$k
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$m

ISSUE:

Whether the exchange of Federal Communications Commission (FCC) radio broadcast station licenses (radio licenses) for an FCC television broadcast station

license (television license) is a like kind exchange subject to the nonrecognition rules under § 1031 of the Internal Revenue Code.

CONCLUSION:

The exchange of FCC radio licenses for an FCC television license is a like kind exchange under § 1031.

FACTS:

Taxpayer is the parent company of an affiliated group that files a consolidated return on a 52-53 week taxable year. X, a subsidiary that was a member of Taxpayer's consolidated group, entered into an asset exchange agreement on Date 1, with Y. Y was subsequently acquired by a consolidated group with Z as the parent company. Pursuant to the agreement, on Date 2, X transferred to Y radio station A in City P, radio station B in City Q, and radio station C in City R, and acquired from Y television station D in City S.

Taxpayer reported for financial reporting purposes that the television station acquired in the exchange had a fair market value of $h, while the radio stations surrendered in the exchange had a basis of $i. Taxpayer, therefore, reported a pre-tax, non-cash, non-operating gain of $j for financial reporting purposes. The FCC licenses represented the largest portion of the exchange with the FCC radio licenses valued at $k and the FCC television license valued at $l.[1]

For federal income tax purposes, Taxpayer treated the exchange of FCC radio licenses for the FCC television license as an exchange of like kind property under § 1031(a). Taxpayer on its consolidated return reported a gain of approximately $m on the exchange, the difference between the reported values of the FCC radio licenses surrendered in the exchange and the FCC television license received in the exchange.

As part of the asset exchange agreement, X transferred tangible property to Y and received tangible property from Y. The bulk of such property was radio and television broadcasting equipment that was in the same product class as set forth in the 1987 Standard Industrial Classification ("SIC") Manual. That product class is SIC code number 3663, which is entitled "Radio and Television Broadcasting and Communications Equipment." Certain other equipment transferred by X and Y pursuant to the asset exchange agreement, including towers used to hold radio and television broadcast equipment, was in the same product class as set forth in the SIC Manual. For federal income tax purposes, Taxpayer treated the exchange of this tangible

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[1] The questions of valuation and/or allocation of value of the FCC licenses are not at issue in this technical advice request.

property as qualifying under § 1031(a).[2]

The Communications Act of 1934 (the "Communications Act") grants the FCC the power to license "radio stations." 47 U.S.C. § 303(a) (1995 & 1999 Supp.). Under this grant of authority, the FCC licenses both radio and television broadcasting. FCC regulations define "radio station" as "[a] separate transmitter or group of transmitters under simultaneous common control, including the necessary equipment required for carrying on a radio communications service." 47 C.F.R. § 1,907. FCC regulations define "radio communication" to mean "[t]elecommunication by means of radio waves," which applies to both radio and television broadcasting. 47 C.F.R. § 2.1. Thus, both radio and television are transmitted over the electromagnetic spectrum by radio transmitting equipment. The Communications Act further grants the FCC the power to "assign frequencies for each individual station and determine the power which each station shall use and the time during which it may operate." 47 U.S.C. § 303(c) (1995 & 1999 Supp.).

The usable radio frequencies of the electromagnetic spectrum range from about 30,000 hertz to 30 gigahertz. Radio broadcasts can be transmitted over frequencies as low as 30 - 300 kilohertz (low frequency) to 300 - 3,000 megahertz (ultra high frequency, "UHF"). Television broadcasts can be transmitted over frequencies as low as 30 - 3000 megahertz (very high frequency, "VHF") to 300 - 3,000 megahertz (UHF). There are 12 VHF channels and 56 UHF channels.

The bandwidth of a radio frequency dictates the amount of information that the frequency can carry. Due to the complexity of a television signal, a much larger bandwidth is needed in comparison to an audio only signal. In the United States, a television channel occupies a width of six megacycles in the radio spectrum. This is 600 times as wide as the channel used by each standard sound broadcasting station.

The rights conferred upon holders of FCC licenses (both radio and television) are described in the FCC licenses themselves. Each of the licenses submitted by Taxpayer expressly states that "the licensee is hereby authorized to use and operate the radio transmitting apparatus herein described." More specifically, each of the FCC licenses confers a right to use the radio transmitting apparatus to broadcast on a designated channel and frequency range, at designated hours of operation, at designated geographic locations, at a maximum effective radiated power, and using antenna with certain antenna system specifications.

Section 301 of the Communication Act confirms that the licenses themselves confer the rights held by licensees. Section 301 provides:

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[2] The treatment of the exchange of tangible personal property is not at issue in this technical advice request.

> It is the purpose of this chapter, among other things, to maintain control of the United States over all the channels of radio transmission, and to provide for the use of such channels, but not the ownership thereof, by persons for limited periods of time, under licenses granted by Federal authority, and *no such licenses shall be construed to create any right, beyond the terms, conditions, and periods of the license*. 47 U.S.C. § 301 (1995 & 1999 Supp.) (emphasis added).

The FCC licenses (both radio and television licenses) submitted by Taxpayer reflect the mandate of § 301 in the following language:

> This license shall not vest in the licensee any right to operate the station nor any right in the use of the frequency designated in the license beyond the term hereof, nor in any other manner than authorized herein.

Thus, the FCC licenses themselves contain the rights to use radio transmitting apparatus to broadcast programming (whether radio or television) over a portion of the electromagnetic spectrum at a certain power in a designated geographic area.

LAW AND ANALYSIS:

Section 1031(a)(1) provides generally that no gain or loss shall be recognized 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. See also § 1.1031(a)-1(a) of the Income Tax Regulations.

Section 1.1031(a)-1(b) provides that "like kind" refers to the nature or character of the property and not to its grade or quality. One kind or class of property may not, under § 1031, be exchanged for property of a different kind or class. See also § 1.1031(a)-2(a).

Section 1.1031(a)-2(a) provides that personal properties of a like class are considered to be of a "like kind" for purposes of § 1031. In addition, an exchange of properties of a like kind may qualify under § 1031 regardless of whether the properties are also of a like class. In determining whether exchanged properties are of a like kind, no inference is to be drawn from the fact that the properties are not of a like class. Under § 1.1031(b), depreciable tangible personal properties are of a like class if they are either within the same General Asset Class (as defined in § 1.1031(a)-2(b)(2)) or within the same Product Class (as defined in § 1.1031(a)-2(b)(3)).[3]

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[3] Property within a Product Class consists of depreciable tangible personal property that is listed in the 1987 Standard Industrial Classification ("SIC") Manual.

Section 1.1031(a)-2(c)(1) provides generally that an exchange of intangible personal property or non-depreciable personal property qualifies for nonrecognition of gain or loss under § 1031 only if the exchanged properties are of a like kind. No like classes are provided for these properties. Whether intangible personal property is of a like kind to other intangible personal property generally depends on the nature or character of the rights involved (*e.g.,* a patent or a copyright) and also on the nature or character of the underlying property to which the intangible personal property relates. For example, an exchange of a copyright on a novel for a copyright on a different novel is a like kind exchange, but an exchange of a copyright on a novel for a copyright on a song is not a like kind exchange. Section 1.1031(a)-2(c)(3).

In the instant case, the FCC radio licenses and the FCC television license are intangible personal property. Thus, the determination of whether they are like kind depends on (1) the nature or character of the rights involved; and (2) the nature or character of the underlying property to which the intangible personal property relates.

The Nature or Character of the Rights Involved

The FCC licenses at issue in this exchange are labeled either, “Television Broadcast Station License,” “AM Broadcast Station License,” or “FM Broadcast Station License.” Taxpayer argues that, despite the labels, the rights granted in each license are virtually identical and that any differences are merely differences in grade or quality.

The example in the regulations regarding intangible property states that a copyright on a novel is like kind to a copyright on a different novel. See § 1.1031(a)-2(c)(3). In this example, the determination that the copyrights are like kind is based, in part, on a comparison of the nature and character of the rights involved (the copyrights). In the case of a copyright, federal law gives the holder of the copyright certain rights regarding the copyrighted material. Thus, as to the first inquiry, the nature or character of the rights involved, one copyright generally will be like kind to another. In the instant case, the determination of whether the FCC radio licenses are like kind with the FCC television license depends, in part, on the nature or character of the rights involved (the licenses).

We think the nature or character of the rights involved should be determined by looking to the substance of the specific rights granted in the FCC licenses, and not merely the labels. These rights are granted by the federal government, which, on behalf of the public, manages and controls the use of the electromagnetic spectrum. The government delegates authority to the FCC to issue licenses to radio and television stations to use the electromagnetic spectrum for broadcasting purposes. An FCC license, whether for television or for radio, enables the licensee to broadcast programming to the public free of charge over the electromagnetic spectrum for the duration of the license. One FCC license will differ from another regarding the specific terms and conditions of operation. However, despite these differences, the rights

conferred on an FCC licensee are basically the same.

An examination of the FCC licenses at issue reveals that each of the FCC licenses confers a right to use the referenced radio transmitting apparatus to broadcast on a designated channel and frequency range, at designated hours of operation, at designated geographic locations, at a maximum effective radiated power, and using antenna with certain antenna system specifications. This right is specifically enumerated in each FCC license, regardless of whether the license relates to a television station, an FM radio station, or an AM radio station. Other than the different labels, the only differences between the various FCC licenses are the specific operating parameters (such as frequency, operating hours, power, and antenna information) and geographic location. These differences do not change the nature or character of the rights granted in the licenses, but are merely differences in grade or quality.

The Nature or Character of the Underlying Property

Section 1031 also requires a comparison of the nature or character of the underlying property to which the intangible personal property relates. The example in the regulations states that a copyright on a novel is not like kind to a copyright on a song. See § 1.1031(a)-2(c)(3). In that example, the underlying properties to which the copyrights relate are the novel and the song, since these are the properties protected by the copyrights. It is the fact that a novel and a song are not like kind that causes these two intangible properties to be not like kind. In the instant case, it is not as clear what property constitutes the underlying property to which the FCC licenses relate.

The agent contends that the exchange of the FCC licenses involves an exchange of a “bundle of rights” represented by the entire array of underlying tangible and intangible properties, which themselves must be examined on a case by case basis. Thus, in the agent’s view, the property underlying the FCC license is all of the station’s radio or television property. This property would include items such as programming content, advertising contracts, market growth, underdeveloped cable television markets, talent contracts, population base, favorable franchise fees, favorable systems performance, etc. The agent provides a detailed comparison of the various characteristics and assets of a radio station and a television station, and concludes that these characteristics and assets are very different. For example, unlike the television business where network affiliation is critical, most radio programming originates locally, and network affiliation has little effect on a radio station’s competitive position.

Taxpayer, on the other hand, argues that the underlying property to which the licenses relate is the tangible personal property referred to in the licenses, i.e., the radio transmitting apparatus consisting of transmitters, towers, and antenna. Taxpayer asserts that this equipment is like kind because it is described in the same Product

Class as in the SIC Manual.[4] Taxpayer argues that the broadcasting equipment is the appropriate property to be examined for purposes of applying this prong of the like kind test for intangible property because this equipment is specifically referred to in the licenses themselves and thus, relates to the "essence" of the licenses.

We must reject the agent's argument as contrary to the approach generally taken in the regulations and revenue rulings, which require that, in determining whether an exchange of businesses qualifies as a like kind exchange, the underlying assets must be analyzed. See § 1.1031(j)-1(a) (requiring the use of exchange groups as an exception to the general rule that § 1031 requires a property-by-property comparison); see also Rev. Rul. 89-121, 1989-2 C.B. 203 (the determination of whether § 1031 applies to an exchange of the assets of one television station for another requires an analysis of the underlying assets exchanged); Rev. Rul. 72-151, 1972-1 C.B. 225 (when an exchange involves multiple assets, the fact that the assets in the aggregate comprise a business does not cause the exchange to be treated as a disposition of a single property for purposes of § 1031). It is no more appropriate to look to the entirety of the assets comprising the radio or television station to determine what is the nature or character of the underlying property of an FCC license, on the grounds that the license is necessary to operate the television or radio station or is the single most valuable asset owned by the station, than it is to view the exchange of a radio or television station as the disposition of a single asset simply because those assets comprise a business or integrated economic investment. See Rev. Rul. 89-121.

A copyright for a novel would expressly reference the underlying novel and a copyright for a song would expressly reference the underlying song. Thus, we agree with Taxpayer's argument that the appropriate manner of identifying the underlying property is to look to the licenses themselves. However, we disagree that the radio transmitting apparatus described in the licenses should be considered the underlying property. Although the licenses specifically authorize Taxpayer to "use and operate the radio transmitting apparatus herein described," we think the license principally relates to the use of the radio transmitting apparatus, rather than the apparatus itself. An FCC license does not authorize the licensee to own or possess radio transmitting apparatus; the licensee would not need an FCC license for the apparatus unless it wanted to use that apparatus to broadcast over the electromagnetic spectrum. The FCC has the specific power to "assign frequencies for each individual station and determine the power which each station shall use and the time during which it may operate." 47 U.S.C. § 303(c) (1995 & 1999 Supp.). An FCC license reflects the FCC's decision to

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[4] Specifically, Product Class 3663, which is entitled "Radio and Television Broadcasting and Communications Equipment," lists "Transmitting apparatus, radio and televison" and "Antennas, transmitting and communications." The towers used to hold the broadcast equipment are listed under "Transmission; prefabricated metal," in Product Class 3441, entitled "Fabricated Structural Metal."

assign a specific frequency of the electromagnetic spectrum to a particular licensee in a given broadcast area. Thus, although an FCC license clearly regulates the manner in which the licensee may use its radio transmitting equipment, we think that the assigned frequency of the electromagnetic spectrum referred to in each license is the underlying property to which the license relates.

Having identified the property underlying an FCC license as the assigned broadcast frequency of the electromagnetic spectrum, we must determine whether the differences between a frequency assigned for television broadcasts and a frequency assigned for radio broadcasts are differences in nature or character or are merely differences in grade or quality.

Several courts have spoken to the meaning of the like kind standard. According to the Court of Appeals for the Fifth Circuit, "the distinction intended and made by the statute is the broad one between classes and characters of property, for instance, between real and personal property." Commissioner v. Crichton, 122 F.2d 181, 182 (5th Cir. 1941), aff'g 42 B.T.A. 490 (1940). The Tax Court has stated that "[t]he comparison should be directed to ascertaining whether the taxpayer, in making the exchange, has used his property to acquire a new kind of asset or has merely exchanged it for an asset of like nature or character." Koch v. Commissioner, 71 T.C. 54, 65 (1978), acq., 1979-1 C.B.1.

Published Service positions, particularly in the area of tangible personal property, have been more restrictive in interpreting the like kind standard. For example, compare Rev. Rul. 79-143, 1979-1 C.B. 264 (U.S. $20 gold coins, which are numismatic-type coins, are not like kind to South African Krugerrand gold coins, which are bullion-type coins), with Rev. Rul. 76-214, 1976-1 C.B. 218 (Mexican 50-peso gold coins and Austrian 100-corona gold coins, both of which are official government restrikes and noncurrency bullion-type coins, are like kind). See also California Federal Life Insurance Co. v. Commissioner, 680 F.2d 85, 87 (9th Cir. 1982), aff'g 107 T.C. 107 (1981) (Tax Court did not err in refusing to apply the lenient treatment of real estate exchanges to an exchange of personal property involving U.S. Double Eagle $20 gold coins and Swiss francs). See generally § 1.1031(a)-2(a) and (b), establishing additional rules for determining the like kind status of tangible depreciable personal property. These authorities indicate that functional differences between seemingly similar properties can be relevant in determining whether two properties are like kind. Similar concerns led Congress to clarify the like kind standard by enacting § 1031(e), which provides that livestock of different sexes are not like kind. See S. Rep. No. 91-552, 91st Cong., 1st Sess. 102 (1969), 1969-3 C.B. 423, 488-489 (in typical cattle operation, male calves are castrated and sold for beef whereas female calves are used for breeding).

In comparing the nature or character of the frequency referred to in each FCC license, it is clear that there are differences between a radio frequency and a television

frequency. As noted above, radio and television broadcasts are assigned to different frequency bands of the usable radio frequency spectrum. Television broadcasts require a considerably larger bandwidth than audio only radio broadcasts. Moreover, a licensee would be in violation of its license if it used a television frequency to broadcast radio transmissions and vice versa. However, even the narrowest interpretation of the like kind standard does not require that one property be identical to another or that they be completely interchangeable. Thus, we find that the differences in the assigned frequencies are not differences in nature or character, but are merely differences in grade or quality. Accordingly, Taxpayer's exchange of FCC radio licenses for an FCC television license qualifies as a like kind exchange under § 1031.

CAVEAT(S)

A copy of this technical advice memorandum is to be given to Taxpayer. Section 6110(k)(3) provides that it may not be used or cited as precedent.