

LET THE BARTERER BEWARE

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In this current trough in the business cycle, many people who find themselves struggling with less disposable income are resorting to “barter” to meet their consumptive needs. The term, “barter,” refers to a “swap,” or exchange, of goods or services without exchange of currency, although in some cases barter is made using goods or services of unequal value, with the recipient of the higher value making up the difference with cash.

News agencies have reported an increase in activity on bartering websites and in the proliferation of bartering clubs, which have been attributed to recession economics. From the relatively simple exchange of professional services, for example, an accountant’s services preparing an annual tax return in exchange for a plumber installing a washer and dryer, to an exchange of real property, for example, a growing family exchanging homes with aging parents seeking to downsize, bartering is becoming a more popular option. This is especially true for those who may be having difficulty obtaining conventional financing for their purchases or for those who cannot easily pinpoint a cash value for their goods in a declining market.

What some people may not realize, however, is that while bartering may not involve payment of cash, you may nonetheless be responsible to pay taxes on the exchange. The fair market value at the time of receipt of the good or service you receive is reportable income to you. Bartering activities may subject you to liabilities for income tax, self-employment tax, employment tax, or excise tax, and may result in ordinary business income, capital gains or capital losses, or you may have a nondeductible personal loss. The IRS recommends you treat barter income as you would any other business activity. Bartering activities must be reported on specific IRS forms depending on the type of thing being exchanged and the commercial setting. It is advisable to consult a tax professional when questions arise about bartering activities.

Bartering websites often use “Trade Dollars” or “Barter Dollars” as the basis of the value of goods or services permitting barter to take place non-simultaneously. For example, if a contractor wanted to barter a \$5,000 roofing repair job on a bartering website, he would earn \$5,000 worth of credits upon contracting for the job, which he could exchange for another good or service worth an equal or lesser value of credits, to be used simultaneously or at a later time from another person in the bartering network, not necessarily the person to whom he sold his services. These trade credits are considered taxable income when they are earned, just as though the contractor had performed the work in exchange for cash.

In addition, it is important to keep in mind that exchanges of “real property” (*i.e.*, land and buildings) may be subject to complex tax rules, for example, Rule 1031 Tax Free Exchanges and non-exempt property exchanges, which can subject the parties involved to very substantial tax liabilities. It is always prudent to retain counsel to advise on any exchanges of real property.

While bartering has its roots in ancient and more primitive cultures, under the Tax Code it is not necessarily a simple practice.