

Chapter C9 Partnership Formation and Operation

Problems

C9-26 a. Neither partner recognized gain nor loss (Sec. 721).

	<u>Suzanne</u>	<u>Bob</u>
Basis of contributed property	\$59,000	\$95,000
Minus: Partnership assumption of individual liabilities		(80,000) ^a
Plus: Share of partnership liabilities	<u>40,000</u>	<u>40,000</u>
Basis in partnership	<u>\$99,000</u>	<u>\$55,000</u>

^aBob's basis also can be determined by reducing the basis of his contributed property by the liabilities assumed by the other partner (\$95,000 - \$40,000 = \$55,000).

c. The partnership takes a carryover basis in each asset: inventory (securities), \$14,000; land, \$45,000; and building, \$50,000.

d. Amount realized	\$20,000
Minus: Adjusted basis	(14,000)
Realized gain	<u>\$ 6,000</u>

Precontribution gain of \$1,000 (\$15,000 FMV at contribution - \$14,000 basis) is allocated to Suzanne. The remaining \$5,000 gain is shared equally by Bob and Suzanne. Suzanne reports \$3,500 of gain and Bob reports \$2,500 of gain. The gain is ordinary (and not capital) because the property was inventory to Suzanne and because the partnership sold the inventory within five years of its contribution. pp. C9-5 through C9-10 and C9-20 through C9-21.

C9-28 a. Julie and Kay recognize no income on the partnership formation. Susan recognizes ordinary income equal to the value of the partnership interest received, or \$30,000.

b.

	Julie	Kay	Susan
Basis of property contributed	\$ -0-	\$80,000	N/A
Plus: Share of liabilities	27,000	36,000	\$27,000
Minus: Liabilities assumed by partnership		(90,000)	
Plus: Income recognized			<u>30,000</u>
Basis in partnership interest	<u>\$27,000</u>	<u>\$26,000</u>	<u>\$57,000</u>

- c. Accounts receivable \$ -0-
 Land 50,000
 Building 30,000
 Organizational expenditure 30,000

d. All of Kay's precontribution loss is allocated to her, and the remaining loss, if any, is shared ratably among the three partners.

	Julie (30%)	Kay (40%)	Susan (30%)	Total (100%)
Precontribution loss*		\$30,000		\$30,000
Postcontribution loss**	<u>\$ 600</u>	<u>800</u>	<u>\$ 600</u>	<u>2,000</u>
Total loss	<u>\$ 600</u>	<u>\$30,800</u>	<u>\$ 600</u>	<u>\$32,000</u>

*\$50,000 basis - \$20,000 FMV = \$30,000 precontribution loss.

**\$20,000 FMV - \$18,000 sales price = \$2,000 postcontribution loss.

pp. C9-5 through C9-12, C9-18 and C9-19.

pp. C9-5 through C9-12.

C9-31 a.

			Possible Tax Year-ends					
			6/30		9/30		10/31	
Partner Name	Partnership Interest	Tax Year	Months Deferred	Total	Months Deferred	Total	Months Deferred	Total
Beth	1/3	6/30	0	.00	9	3.00	8	2.67
Cindy	1/3	9/30	3	1.00	0	.00	11	3.67
Delux	1/3	10/31	4	<u>1.33</u>	1	<u>.33</u>	0	<u>.00</u>
				<u>2.33</u>		<u>3.33</u>		<u>6.34</u>

The partnership must use a June 30 year-end, or with a Sec. 444 election, a tax year that ends on March 31, April 30, or May 31.

b. The natural business year that ends on January 31.

c. The partnership would be required to use an October 31 year-end, or the tax year of the majority partner. Alternatively, if IRS permission was received, a natural business year-end (January 31) could be used, or with a Sec. 444 election, a tax year that did not exceed a three-month deferral of income could be used. pp. C9-12 through C9-15.

C9-32 a. The tax year-end of majority partners Bipin and Damien is December 31, and this is the required year-end for the partnership.

b. Yes. Possible year-ends are those that allow for no more than a three-month deferral from the required December 31 year-end. These year-ends include September 30, October 31, and November 30. pp. C9-12 through C9-15.

C9-33 a. Separately stated items:

Dividends	\$ 19,000*
Municipal bonds interest	18,000
Corporate bond interest	29,000*
Precontribution gain on land specially allocated to Karen	25,000**
Sec. 1231 loss	28,000
Net long-term capital loss	4,000
Short-term capital losses	5,000
Charitable contributions	23,000
Investment interest expense	16,000*
Guaranteed payment to Karen	37,000
Rehabilitation expenditure	164,000

*Items that must be separately stated so that investment interest limitation and portfolio income can be properly reported by the partners.

**The land was held by Karen as inventory and therefore will generate \$40,000 of ordinary income if sold by the partnership within five years of the contribution. All precontribution gain (\$25,000) must be allocated to Karen while the remaining \$15,000 of postcontribution gain is shared by all of the partners in Part b.

b. KLM's ordinary income:

Operating profit minus guaranteed payment (\$120,000 - \$37,000)	\$83,000
Postcontribution gain on land contributed by Karen	15,000
MACRS depreciation allowance	<u>(36,000)</u>
Ordinary income	<u>\$62,000</u>

pp. C9-15 through C9-20.

C9-34

Transaction	Book Income	(a) Taxable Income	(b) Ordinary Income	(c) Separately Stated Items
INCOME				
Operating Profit	\$ 94,000	\$ 94,000	\$ 94,000	
Rental income	30,000	31,000*		\$ 31,000
Interest municipal bonds	15,000			15,000
Interest corporate bonds	3,000	3,000		3,000
Dividend	20,000	20,000		20,000
Gain on investment land	60,000	66,000 ^b		66,000 ^c
LTCG	10,000	10,000		10,000
STCL	(7,000)	(7,000)		(7,000)
Sec. 1231 gain	9,000	9,000		9,000
Sec. 1251 gain	44,000	44,000	44,000	
EXPENSES				
Depreciation	(39,000)	(41,000) ^d	(29,000)	12,000
Interest:				
Mortgage	(18,000)	(18,000)		(18,000)
Mun. bond loan	(5,000)			(5,000)
Guaranteed payment	(30,000)	<u>-0-</u> ^e	(30,000)	30,000
TOTAL	<u>\$186,000</u>	<u>\$211,000</u>	<u>\$ 79,000</u>	

^a Prepaid rental income is reported for tax purposes when it is received.

^b For financial accounting purposes, the basis of the land was \$15,000 and gain of \$60,000 was reported. The tax basis was \$6,000 smaller so the tax gain would be \$6,000 larger.

^c The precontribution gain of \$6,000 (\$15,000 - \$9,000) must be specially allocated to Jim while the postcontribution gain of \$60,000 (\$66,000 total gain - \$6,000 precontribution gain) is allocated ratably to all three partners.

^d MACRS depreciation is used for tax purposes.

^e Note that the guaranteed payment has no net effect on taxable income. The guaranteed payment both reduces ordinary income and increases separately stated income items that are taxable.

Each partner will be notified of his share of low income housing expenditures qualifying for the credit.

pp. C9-15 through C9-20.

C9-35 a.

Items	Partner			
	Total	Becky	Chuck	Dawn
Ordinary income	\$120,000	\$24,000	\$36,000	\$60,000
Long-term capital gain	18,000	3,600	5,400	9,000
Short-term capital loss	6,000	1,200	1,800	3,000
Charitable contribution deduction	20,000	4,000	6,000	10,000

b.

	Partnership Total	%	Becky's Amount	%	Chuck's Amount
1/1 through 6/30^a					
Ordinary income	\$59,507	20%	\$11,901	30%	\$17,852
LTCG	8,925	20%	1,785	30%	2,678
STCL	2,975	20%	595	30%	893
Charitable contribution	9,918	20%	1,984	30%	2,975
7/1 through 12/31^b					
Ordinary income	\$60,493	25%	\$15,123	25%	\$15,123
LTCG	9,074	25%	2,269	25%	2,269
STCL	3,025	25%	756	25%	756
Charitable contribution	10,082	25%	2,521	25%	2,521

^a1/1 through 6/30 is 181 days in a non-leap year.

^b7/1 through 12/31 is 184 days in a non-leap year.

pp. C9-17 and C9-18.