Updates to Section III: Subchapter K Partnerships

Page 6779-80: Replace sections (a) and (b) with the following:

Proposed regulations provide that for a guarantee to be recognized under section 752, it must be triggered by the first dollar of loss sustained by the benefitting party. For an example of a guarantee that will not be recognized, consider the following: "I will reimburse you, the debtor, on your obligation of $1,500, but only to the extent you are forced to pay more than $1,000." Because this guarantee is not triggered until the debtor (that is, the benefitting party) loses more than $1,000, it will be ignored under section 752. The only exception to this rule is when such a guarantee covers at least 90% of the total obligation (meaning it starts no later than after the first 10% of loss).

Page 782: Replace the first paragraph of section 6 with the following:

Under section 708(b)(1), a partnership terminates if "no part of any business . . . continues to be carried on by any of its partners in a partnership."[1] Note that because a partnership requires two or more partners, §761, acquisition by one partner of all the interests of the other partners terminates the partnership as does acquisition of all the partnership interests by a single acquiror. Treas. Regs. §1.708-1(b)(1)(i).

Page 782 ; Delete the last full paragraph as well as the paragraph that starts on page 782 and carries over to page 783.

Page 785: Delete note 2.

Pages 785-86: Replace problems 25-8 and 25-9 with the following:

25-8. Individuals X and Y equally own XY-LLC, a limited liability company taxable as a partnership. and individual Z owns Z-LLC, a limited liability company treated as a disregarded entity. XY-LLC owns a single asset (Blackacre) that consists of a parcel of domestic real estate. Z-LLC owns a single asset (Whiteacre), also consisting of a parcel of domestic real estate. What are the tax consequences to X, Y and Z if X and Y transfer their interests in XY-LLC to Z in exchange for all of Z's interests in Z-LLC (half transferred to X and half to Y)?

[1] Prior to enactment of the Tax Cut and Jobs Act of 2017, a partnership also would terminate if interests representing more than a specified percentage of profits and capital were sold exchanged in a 12-month period (such a termination was called a "technical" termination).

25-9. If the owners of a partnership wish to incorporate the partnership's business, how might the transaction be structured? What tax consequences should follow from each possible form? Consider Rev. Rul. 84-111, 1984-2 C.B. 88.

Page 814: Add the following to the end of subsection c:

The Tax Cut and Jobs Act of 2017 dramatically expanded the reach and impact of bonus depreciation in section 168(k). Now, the cost of property that qualifies for bonus depreciation can be deducted in full in the year of acquisition (formerly, only 50% of the cost could be expensed).[2] Further, used property now can qualify for bonus depreciation, subject to an anti-churning rule in §168(k)(2)(E)(ii).

If a positive basis adjustment is allocable to property qualifying for bonus depreciation, can the positive basis adjustment itself qualify for bonus depreciation? The answer seems to be no because of the anti-churning rule: while the basis adjustment is treated as property newly placed in service, presumably the partnership will be treated as having been used by the partners in the past. See §168)k)(2)(E)(ii)(I).

Page 828: Add the following after the carryover paragraph at the top of the page:

The Tax Cut and Jobs Act of 2017 dramatically expanded the reach and impact of bonus depreciation in section 168(k). Now, the cost of property that qualifies for bonus depreciation can be deducted in full in the year of acquisition (formerly, only 50% of the cost could be expensed).[3] Further, used property now can qualify for bonus depreciation, subject to an anti-churning rule in §168(k)(2)(E)(ii).

If a positive basis adjustment is allocable to property qualifying for bonus depreciation, can the positive basis adjustment itself qualify for bonus depreciation? If the transferee partner had no direct or indirect interest in the partnership prior to acquisition of the partnership interest, then the answer should be that the positive basis adjustment *can* qualify for immediate expensing under §168(k)(8).

Recall that section 743(b) operates to give the transferee partner a cost basis in the transfereer's share of each of the partnership's assets (at least when the acquisition is fully taxable to the transferor partner). Had the transferee purchased a share of each asset directly, then application of §168(k) would be automatic (assuming all the requirements of that section are satisfied). To ensure that section 743(b) fully duplicates a direct asset acquisition, section 743(b) should apply to the basis step-up. Note also that the transferor partner is taxed under the §751(a) regulations as if they assets were sold, further supporting the treatment of the buyer as effectively purchasing a share of the partnership's assets.

Page 830: Replace the final sentence of the carryover paragraph (the first paragraph of Note 1) with the following:

[2] In general, qualifying property includes depreciable tangible property having a depreciable life of 20 years or less. See §168(k)(2)(A). Thus, real estate is excluded.

[3] In general, qualifying property includes depreciable tangible property having a depreciable life of 20 years or less. See §168(k)(2)(A). Thus, real estate is excluded.

In this context, a partnership has a "substantial built-in loss" if the aggregate basis of the partnership's assets exceeds the fair market value of its assets by more than $250,000, §743(d)(1)(A), or if the transferee's distributive share of loss would exceed $250,000 if the partnership sold all of its assets for fair market value, §743(d)(1)(B). Note that this second test focuses on the adjustment that would be mandated if a §754 election were in effect and so parallels section 734(d)(1). However, the first test looks at the partnership rather than at the transferor partner. In particular, an adjustment triggered by the test in §743(d)(1)(A) can be much smaller than $250,000.