

IRC Section 743(b) Basis Adjustments: Applying the 754 Election to Distributions of Partnership Property

An Advanced Case Study of Calculations and Considerations

TUESDAY, DECEMBER 15 2015, 1:00-2:50 pm Eastern

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IRC Section 743(b) Basis Adjustments

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Robert S. Barnett

Capell Barnett Matalon & Schoenfeld

rbarnett@cbmslaw.com

Janice H. Eiseman

Cummings & Lockwood

jeisem@cl-law.com

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IRC Section 743(b) Basis Adjustments

Janice H. Eiseman
Cummings & Lockwood

I. Overview

- A. **Subchapter K:** In parts of Subchapter K, the subchapter governing the taxation of partnerships and partners, a partnership is treated as a separate *entity*, which is distinct from its partners. In other parts of Subchapter K, a partnership is treated as an *aggregate* of individuals, each of whom owns an undivided interest in partnership assets.

- B. **Outside Basis:** “Outside basis” refers to a partner’s tax basis in the partnership interest itself. The partnership is treated as an *entity* separate from its partners and the partnership interest as an intangible asset that is separate and distinct from partnership assets. This is similar to a shareholder’s tax basis in a share of stock.

Overview (Cont.)

- C. Inside Basis:** “Inside basis” refers to the partner’s share of the basis in the assets held by the partnership. Because the partnership is not a separate taxable entity, its income is allocated and taxed to its partners, treating them like owners of undivided interests in the assets and business of the partnership, i.e., as an *aggregate* of individuals. This does not have a direct analog in the Subchapter C or Subchapter S world because corporations are treated as separate entities.
- D. Benefit of Partnership Taxation:** By making a Code Section 754 election, the partnership tax law allows the “outside basis” and the “inside basis” to be equal. What this means is the following: If the partnership were liquidated for cash immediately after the event causing the Section 754 election for an amount equal to the outside tax basis to the partner for whom the election applies, that partner would recognize no gain or loss from the sale of the partnership assets or from the liquidating distribution.

§754

By Robert S. Barnett

CPA, JD, MS (TAXATION)

CAPELL BARNETT MATALON & SCHOENFELD, LLP.

ATTORNEYS AT LAW

(516) 931-8100

rbarnett@cbmslaw.com

OVERVIEW

TWO BASIS CONSIDERATIONS

1. **OUTSIDE BASIS** – The adjusted basis of the partnership interest held by a partner
2. **INSIDE BASIS** – The adjusted basis of assets held by a partnership (ex. building)
 - Corporate shareholders have similar considerations
 - Partnerships have special rules

OUTSIDE BASIS

- Partners have a **single** outside basis
- Determines gain/loss on sale
- Affects consequences of partnership distributions
- Determines deductibility of losses
- Corporate shareholders have separate basis for each block

§705

- Outside basis is increased by share of income and contributions
- Decreased by share of losses/distributions
- Not Below Zero
- Balance is often present
- Basis determined without reference to capital account

EXAMPLE 1

- A contributes property adjusted basis = \$400
FMV=\$1,000
- B Contributes \$1,000
- Under agreement A's capital account is \$1,000
- But A's basis = \$400

OFF BALANCE

- Sale of a partnership – purchaser's outside basis is initially cost
- Death of a partner – step-up in outside basis

EXAMPLE 2

A \$50,000 50%

B \$50,000 50%

Purchase Building \$100,000

Building doubles in value

C Purchases B's interest for \$100,000

EXAMPLE 2 Continued

B reports \$50,000 gain

C's outside basis \$100,000

A's outside basis \$50,000

Total inside basis \$100,000

C's share of inside basis \$50,000

EXAMPLE 2

- **OUT OF BALANCE**
- §743(a) – Basis of partnership property – generally not adjusted as a result of a transfer of a partnership interest (or a distribution of partnership property §734(a))

§742

- Basis of transferee partner's interest in partnership is determined under general rules
- §1011 cost; from a decedent FMV and share of liabilities- IRD

ENTITY APPROACH

- §743(a) follows entity approach
- General rule views the partnership as an entity distinct from its partners
- Acquirer would not receive a basis adjustment in partnership assets
- Corporation is similar

§754 ELECTION

BALANCE

- Upon sale or exchange or upon death §743(b)
- §734(b) upon distribution of property to a partner
- Basis of partnership property is adjusted
- Provided §754 election is made
- Adjustment may be positive or negative

§743(b) BASIS ADJUSTMENT

- Protects purchasing partner
- “As If” purchased a pro rata interest in partnership assets
- Only for transferee partner

§754

- If partnership files an election
- In accordance with regulations
- Basis of partnership property
- Is adjusted
- As provided in §734 and §743

EXAMPLE 2 Continued

- If §754 election
- C receives inside basis in the real property of \$100,000 – C paid for the adjustment
- Binding on partnership in year of election and all subsequent years
- May result in a positive or negative basis adjustment
- **Positive adjustment:** o/s basis is $>$ adjusted basis of partnership property

WHAT HAPPENS UNDER §743(b)?

HARMONY & BALANCE

- Inside/Outside
- C gets the benefits he paid for – depreciation – less gain if asset is sold
- Estate receives ability to sell without double tax

§743 BASIS ADJUSTMENT

- **DIFFERENCE BETWEEN** transferee's initial basis for partnership interest and transferee's proportionate share of the adjusted basis of partnership property
- In our example, the \$50,000 difference
- Follows the aggregate approach

POSITIVE/NEGATIVE

- If transferee's basis in Partnership Interest $>$ share of allocable basis of partnership property, the adjustment **increases** the basis of partnership property
- The opposite results in a **decreased** basis – if values are declining and o/s basis $<$ transferee's proportional share of basis in partnership property
- BALANCE GENERALLY ACHIEVED

TAX EFFECT TO TRANSFEREE

- §743(b) **positive basis** adjustments will **reduce** transferee's income
- Increased depreciation deduction
- Reduced allocable gain on sale of partnership assets

EXAMPLE

- Partnership holds appreciated rental properties
- Partner A dies – no §754 election
- Outside basis step-up
- Partnership sells asset A – allocable amount of gain passes to estate – no inside basis increase
- Increases outside basis
- Timing results in future capital loss when interest is disposed of

PRACTICE POINTS

- Send request letter
- Read partnership agreement or operating agreement

DETERMINATION OF INSIDE BASIS

- Share of adjusted basis of partnership property
 - Equals sum of interest in previously taxed capital **PLUS** share of partnership liabilities

PREVIOUSLY TAXED CAPITAL

- \$ transferee would receive on a hypothetical liquidation
 - Increased by allocated tax loss
 - Decreased by allocated tax gain

HYPOTHETICAL TRANSACTION

- Disposition of all partnership assets
- Immediately after the transfer
- In a fully taxable transaction
- At FMV

EXAMPLE: §754 ELECTION MADE

- A sells to T for \$22,000

	BASIS	FMV
CASH	\$5,000	\$5,000
A/R	\$10,000	\$10,000
INVENTORY	\$20,000	\$21,000
BUILDING	\$20,000	\$40,000
TOTAL ASSETS	\$55,000	\$76,000
LIABILITIES	\$10,000	\$10,000
CAPITAL – A	\$15,000	\$22,000
CAPITAL – B	\$15,000	\$22,000
CAPITAL – C	\$15,000	\$22,000
TOTAL LIAB/CAPITAL	\$55,000	\$76,000

EXAMPLE continued

- §743(b) basis adjustment = \$7,000
- O/S Basis = \$25,333 (cash + share of liabilities)
- T's interest in taxed capital = \$15,000 (\$22,000 liquidation interest LESS tax gain = \$7,000)
- T's share of liabilities = \$3,333

EXAMPLE continued

- O/S Basis = \$25,333
- Less share of inside basis = \$18,333
- **§743(b) BASIS ADJUSTMENT** \$ 7,000

Effects Of Treasury Reg. 1.743-1(j)

- §743 basis adjustment only affects transferee
- Partnership first computes income at the partnership level.
- Then allocates to partners IRC §704
- Then adjusts capital accounts accordingly
- **Then**, transferee's basis adjustment is reflected on K-1 as an adjustment to distributive share.
- But, adjustments do not affect capital accounts.

WHAT DOESN'T HAPPEN

- **Capital account** of transferor carries over to the transferee
- §743 adjustments are not reflected in the capital account of the transferee
- Also disregard subsequent related adjustments (ex. increased depreciation)
- If purchase an interest subject to §704(c) the §754 election is imperative

TRANSFeree PARTNER

- Must notify the partnership of the transfer
- Within 30 days
- Names, address, TIN of transferor and transferee
- Date of transfer
- Relationship and other tax information (ex. purchase price and liabilities assumed)

PARTNERSHIP

- Also has disclosure rules
- Identify transferee
- Show basis adjustment and allocations

PARTNERSHIP REPORTING

- Identify transferee
- Transferee's TIN
- Computation of Basis Adjustment

Transferee's Basis in Partnership Interest	Transferee's Share of Basis in Partnership Property	Amount of Adjustment
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- Allocation to Partnership Properties

Asset	Basis	FMV	Adjustment Allocation
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Substantial Built-In Loss

- Basis of partnership property is adjusted – **even if** no §754 election
 - Transfer of partnership interest
 - Death of a partner
 - A distribution of property with a substantial basis reduction is treated similarly.

Substantial Built-In Loss (Cont.)

- If the partnership's adjusted basis in all partnership property exceeds FMV by more than \$250,000
- The substantial basis reduction for distributed property is similar.
- Does not apply to securitization partnerships and electing investment partnerships
- IRC §743(d) and §734(d)

Example

- A & B partners: A contributes property – FMV \$500,000, basis \$1,000,000
- B contributes \$500,000 cash. A sells interest to C for \$500,000.
- If §754 election or substantial built-in-loss
- C negative basis adjustment \$500,000
- Will affect C on sale of property
- Offsets §704(c) loss allocated to C

Depreciation Recapture

- Partner reports his/her distributive share of depreciation recapture.
- Based upon total amount of depreciation allowed or allowable allocated to that partner
- On transfer of partnership interest – depreciation recapture allocated to transferee

Effect Of §754 Election

- §743(b) basis adjustment alters result.
- Only depreciation claimed after the date of acquisition of the partnership interest is taken into effect for the recapture computation.

Example

- A & B partnership purchases equipment for \$5,000; 90% depreciation to A, 10% to B
- A receives depreciation on deduction of \$900, B \$100
- Sale of property for \$5,000
- §1245 recapture to A = \$900
- If T purchases A's interest, make sure §754 election is in place
- To minimize recapture

ESTATES SPECIAL RULES

- §1014(a) – generally, basis step-up to FMV (at death or alternate valuation date)
- §1014(c) – **IRD** exception – no step-up for IRD items
- Reg. §1.742-1 – similarly excludes **IRD** and includes successor's share of Partnership liabilities
- **IRD** consists of D's right to income not received before death. Taxed to recipient (estate or beneficiary)

IRD & PARTNERSHIPS

- Treas. Reg. §1.755-1 – “if...the partnership holds assets representing [IRD], no part of the basis adjustment under §743(b) is allocated to these assets. See §1.743-1(b)
- §736(a) – liquidation payments due to D and paid to successor. Reg. 1.753-1
- D’s interest in zero basis A/R and other income rights (some disagreement exists, see §753)

I. Code Section 755 Basis Adjustments

A. Three Sets of Rules:

1. Transfer of partnership interest when assets of partnership do not constitute a trade or business. Treas. Reg. § 1.755-1(b)(1)-(b)(4).
2. Transfer of partnership interest involving “substituted basis exchanges” (e.g., Code Section 351 and 721 exchanges). Treas. Reg. § 1.755-1(b)(5). Also, Treasury Regulation § 1.755-1(b)(5) applies to basis adjustments that result from exchanges in which the transferee’s basis in the partnership interest is determined by reference to other property held at any time by the transferee e.g. a constructive termination under Code Section 708(b)(1)(B) in which the terminated partnership is deemed to contribute its assets to a new partnership in exchange for an interest in the new partnership and the terminated partnership is deemed to distribute interests in the new partnership in liquidation of the partner’s interest in the terminated partnership. Code Section 761(e) provides the “exchange”--the distribution of partnership interests in the new partnership is an “exchange” for purposes of Code Section 743(b). Because the distributee-partner of the terminated partnership receives its interest in the new partnership in a liquidating distribution, the distributee takes a substituted basis in the new partnership under Code Section 732(b). A Code Section 754 election by the new partnership will bring into play Treasury Regulation § 1.755-1(b)(5).
3. Transfer of a partnership interest when the assets of the partnership constitute a trade or business, as described in Treasury Regulation § 1.1060-1(b)(2). Treas. Reg. § 1.755-1(a)(2)-(a)(6).

Code Section 755 Basis Adjustments (Cont.)

B. Transfer of Partnership Interest When Assets of Partnership do not Constitute a “Trade or Business.”

1. First, determine the adjusted basis and the fair market value of the partnership assets immediately after the transfer and determine how much income, gain or loss (including remedial allocations under Treasury Regulation § 1.704-3(d)) would be allocated to the transferee-partner if the partnership were to sell all of its assets for cash in a hypothetical sale for an amount equal to their fair market values. If, in fact, the purchase price for the partnership interest equals the fair market value of the assets, then the adjustment to the basis of partnership property with respect to the transferee-partner is done.
Treas. Reg. § 1.755-1(b)(1)(ii) Example 1, Treas. Reg. 1.755-1(b)(2)(ii).
2. The portion of the transferee-partner’s basis adjustment allocated to ordinary income property is equal to the total income gain or loss (including remedial allocations) that would be allocated to the transferee with respect to the hypothetical sale of ordinary income property. Treas. Reg. § 1.755-1(b)(2).

Code Section 755 Basis Adjustments (Cont.)

3. The portion of the transferee-partner's basis adjustment allocated to capital gain property is equal to the Section 743(b) adjustment reduced by the amount allocated to ordinary income property. If the purchase price of the partnership interest is less than the purchase price based upon fair market value, and there has to be a decrease in capital gain property, the decrease cannot be greater than the "partnership's basis" in the property or the transferee's share of any remedial loss under Treasury Regulation § 1.704-3(d). Any excess is applied to reduce the basis of ordinary income property. Treas. Reg. § 1.755-1(b)(2).
 - Note that this approach allocates any overpayment or underpayment for the partnership interest to the basis of capital gain property.

4. Adjustments can be made to individual assets even though the total amount of basis adjustment is zero. Treas. Reg. § 1.755-1(b)(1)(i). See Exhibit A.
 - Note that in a substituted basis transaction no adjustment can be made if the total amount of the Section 743(b) adjustment is zero.

Code Section 755 Basis Adjustments (Cont.)

5. Allocations have to be made within the class of ordinary income property and within the class of capital gain property.
 - a. Within the class of ordinary income property, the basis of each property is generally adjusted by an amount equal to the income, gain, or loss (including remedial allocations) that would be allocated to the transferee upon a sale of the property in the hypothetical transaction.
 - b. Within the class of capital gain property, the basis of such property is generally adjusted by (1) the amount of income, gain or loss that would be allocated to the transferee in the hypothetical transaction, minus (2) a portion (based on the market value of a particular property) compared to the aggregate market value of all capital gain property. Treas. Reg. § 1.755-1(b)(3).
 - c. Note that there must be an adjustment whenever the actual Code Section 743(b) adjustment is either more or less than what it would be if the transferee had paid fair market value for each partnership asset.
6. See subsequent Exhibits B, C and D for examples of Code Section 755 allocations.

Code Section 755 Basis Adjustments (Cont.)

C. Substituted Basis Exchanges

1. The rules for “substituted basis exchanges” are set forth in Treasury Regulation § 1.755-1(b)(5). If the basis adjustment is positive, an adjustment can be made only if the hypothetical sale of the partnership’s assets results in a net gain to the transferee.
 - a. The increase is allocated between classes of assets, ordinary and capital, in proportion to the net income or gain of each class allocable to the transferee.
 - b. Within each class, increases are first allocated to properties with unrealized appreciation in proportion to the transferee’s share of such unrealized appreciation until the transferee’s share of the appreciation is eliminated; any remaining amount is allocated among assets in the class according to the transferee’s share of the amount realized from the hypothetical sale of each asset in the class.
2. Likewise, if the basis adjustment is negative, an adjustment can only be made if the hypothetical sale results in the allocation of a net loss to the transferee.
 - a. The decrease is allocated between asset classes in proportion to the net loss allocable to the transferee from the hypothetical sale of all assets in each class.
 - b. Within each class, the decrease is allocated to properties with unrealized depreciation in proportion to the transferee’s shares of such unrealized depreciation until they are eliminated; remaining decreases are allocated in proportion to the transferee’s shares of the adjusted bases of all assets in the class until these shares of adjusted bases are reduced to zero, with any remaining downward adjustment suspended until the partnership acquires additional property in that class.

Code Section 755 Basis Adjustments (Cont.)

D. Sale of Business

1. If the assets of the partnership constitute a trade or business (as described in Treasury Regulation § 1.1060-1(b)(2)), the partnership must use the residual method to assign values to the partnership's Section 197 intangibles. Treas. Reg. § 1.755-1(a)(2).
2. Residual method involves the following steps:
 - a. First, the partnership must determine the value of its assets other than Section 197.
 - b. Second, the partnership must determine "partnership gross value" under Treasury Regulation § 1.755-1(a)(4).
 - c. Third, the partnership gross value is then compared to the aggregate value of all partnership property other than Section 197 intangibles. If there is no residual value, then the value of all Section 197 intangibles is deemed to be zero. If there is a residual value, then the amount must be allocated to Section 197 intangibles in order to assign a value to them under the rules of Treasury Regulation § 1.755-1(a)(5).
 - d. "Partnership gross value" generally is equal to the amount that, if assigned to all partnership property, would result in a liquidating distribution to the partner equal to the transferee's basis in the transferred partnership interest immediately following the relevant transfer (reduced by the amount, if any, of such basis that is attributable to partnership liabilities). Treas. Reg. § 1.755-1(a)(4)(i)(A).
 - e. Treasury Regulation § 1.755-1(a)(5)(i) requires that the residual value be allocated first among Section 197 intangibles other than goodwill and going concern value, but the value assigned to a Section 197 intangible (other than goodwill and going concern value) is limited to its actual fair market value on the date of the relevant transfer. Any remaining residual value is then allocated to goodwill and going concern value. See Exhibit E.

Exhibit A

Sale or Exchange when Section 743(b) adjustment is zero. Ex. 2 of Treas. Reg. § 1.755-1(b)(2)(ii):
T buys A's interest for \$1,000.

	Adjusted Basis	Fair Market Value	743(b) Adjustment
Capital Gain Property			
Asset 1	\$500	\$750	\$125
Asset 2	500	500	

Ordinary Income Property			
Asset 3	\$500	\$250	(\$125)
Asset 4	500	500	
	_____	_____	_____
	\$2,000	\$2,000	0
<u>Capital:</u>			
A	1,000	1,000	
B	1,000	1,000	

If there is a sale of partnership property immediately after purchase, then T will not recognize an ordinary loss of \$125.00 and will not recognize a capital gain of \$125.00

Exhibit B

Example 1 of Treas. Reg. § 1.755-1(b)(2)(ii) and Example 1 of Treas. Reg. § 1.755-1(b)(3)(iv):
T buys A's partnership interest for \$120,000 and 110,000, respectively.

	Adjusted Basis	Fair Market Value at time of contribution	Fair Market Value at time of sale	Section 743(b) Adjustment (Ex. 1)	Section 743(b) Adjustment (Ex. 2)
Capital gain property					
Asset 1	\$25,000	\$50,000	\$75,000	\$37,500	\$33,604
Asset 2	\$100,000	\$100,000	\$117,500	\$8,750	\$2,646
			<u>\$192,500</u>	<u>\$46,250</u>	<u>\$36,250</u>
Ordinary Income property					
Asset 3	\$40,000	\$40,000	\$45,000	\$2,500	\$2,500
Asset 4	\$10,000	\$10,000	\$2,500	(\$3,750)	(\$3,750)
	<u>\$175,000</u>	<u>\$200,000</u>	<u>\$47,500</u>	<u>(\$1,250)</u>	<u>(\$1,250)</u>
Total			\$240,000	\$45,000 (ex. 1)	\$35,000 (ex. 2)
Capital					
A	\$75,000	\$100,000			
B	\$100,000	\$100,000			
Section 743(b) adjustment:					
T's partnership basis	\$110,000	\$120,000			
Less: T's share of adjusted basis in partnership property	<u>(\$75,000)</u>	<u>(\$75,000)</u>			
Adjustment	\$35,000	\$45,000			
Ordinary income adjustment	(\$1,250)	(\$1,250)			
Capital gain adjustment	\$36,250	\$46,250			
Total capital gain		<u>Adjustment</u>			
Asset 1	\$37,500	\$33,604	(\$37,500 - (\$10,000 * \$75,000/\$192,500))		
Asset 2	\$8,750	\$2,646	(\$8,750 - (\$10,000 * \$117,500/\$192,500))		
Total capital gain/Adjustment	\$46,250	\$36,250			

Exhibit C

SECTION 743(b) COMPUTATION for REAL ESTATE PARTNERSHIP and SECTION 755 ALLOCATION							
Decedent's Percentage Interest	7.62605%						
Date of Death: December 5, 2009							
	Adjusted Basis of Partnership Assets At Date Of Death	Fair Market Value Balance Sheet	Adjustment to Estate Based Upon Hypothetical Sale At Fair Market Value	Decrease Based Upon Value At Date Of Death Of Partnership Interests*	Adjustment to Gain or Loss	Estate's Basis Inside Partnership Prior To Adjustment	Estate's Basis Inside Partnership After Adjustment
ASSETS							
Cash & Equivalents	1,793,186	1,793,186	0	0	0	136,749	136,749
Prepaid Expenses	174,647	174,647	0	0	0	13,319	13,319
Mortgage Escrow	107,564	107,564	0	0	0	8,203	8,203
Repair Reserve	2,504	2,504	0	0	0	191	191
Due from Others	14,900	14,900	0	0	0	1,136	1,136
Security Deposits	132,031	132,031	0	0	0	10,069	10,069
Current & Other Assets	2,224,832	2,224,832	0	0	0	169,667	169,667
Buildings & Other Depreciable Assets	17,725,575	20,960,000					
Less: Accumulated Dep. & Amort.	15,000,000	0					
Net Buildings & Other Depreciable Asset	2,725,575	20,960,000	1,390,566	247,445	1,143,121 (A)	207,853	1,350,974
Land	341,864	5,240,000	373,534	61,861	311,673 (B)	26,071	337,744
Intangible Assets	323,497	0					
Less: Accumulated Amortization	0	0					
Total Net Intangible Assets	323,497	0	(24,670)	0	(24,670)	24,670	0
Total Assets	<u>5,615,768</u>	<u>28,424,832</u>	<u>1,739,431</u>	<u>309,307</u>	<u>1,430,124</u>	<u>428,261</u>	<u>1,858,385</u>
LIABILITIES							
Due to Others	9,056	9,056	691			691	691
Security Deposits	131,203	131,203	10,006			10,006	10,006
All Nonrecourse Loans	18,000,000	18,000,000	1,372,689			1,372,689	1,372,689
Total Liabilities	18,140,259	18,140,259	1,383,385			1,383,385	1,383,385
Members Equity (Deficit)	(12,524,491)	10,284,573	356,046			(955,124)	475,000
Total Liabilities & Members Equity	<u>5,615,768</u>	<u>28,424,832</u>	<u>1,739,341</u>			<u>428,261</u>	<u>1,858,385</u>

Exhibit C (cont'd)

Code Section 743(b) Adjustment									
Tax Basis of Partnership Interest for Decedent									
Code Section 1014 tax basis (outside basis)		475,000.00							
Share of liabilities		<u>1,383,385.00</u>							
Total		1,858,385.00							
Less:									
Previously taxed capital		(955,124.00) *							
Share of liabilities		<u>1,383,385.00</u>							
Share of tax basis of Partnership property (inside basis)		428,261.00							
Section 743(b) Adjustment		1,430,124.00							
*Decedent's interest in Partnership previously taxed capital:									
Cash received upon liquidation of partnership at fair market value		784,306.68							
Less: Gain allocated to decedent from liquidation		<u>1,739,430.68</u>							
		(955,124.00)							
Adjustment= (Hypothetical adjustment of asset-((Total Hypothetical Adjustment-Total Actual Adjustment)*FMV Asset/Total FMV))									
(A) Bldg: $\$1,390,566 - ((1,739,431 - 1,430,124) * 20,960,000/\$26,200,000)$ = \$1,143,121									
(B) Land: $\$373,534 - ((1,739,431 - 1,430,124) * 5,240,000/\$26,200,000)$ = \$ 311,673									

Exhibit D

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Example of complicated adjustment for an interest held by a Grantor Trust upon death of Grantor; value of membership interest determined for estate tax purposes.

Calculation of Section 743(b) Adjustment to Trust			
I. Step-up in basis of Company assets based on <u>fair market value</u> at date of death			
Proportionate Share of Tax Basis in Company's Assets		Gain recognized upon liquidation	Code § 743(b) Basis Adjustment & Code § 755 Allocation
Real Estate	\$173,500	\$17,826,500	\$17,826,500
Accrued Dividend	0	\$578	0
Sysco	0	\$37,129	\$37,129
Johnson & Johnson	0	\$15,242	\$15,242
Schering Plough	0	\$10,379	\$10,379
United Health Care	0	\$6,226	\$6,226
Cisco	0	\$18,306	\$18,306
Dover	0	\$13,729	\$13,729
Emerson	0	\$11,295	\$11,295
Bershire Hathaway A	0	\$46,525	\$46,525
Berkshire Hathaway B	0	\$30,462	\$30,462
	\$173,500	\$18,016,371	\$18,015,793
(Stock contributed by children of grantor of Trust)			
II. Trust's previously taxed capital:			
		Liquidation proceeds based on fair market value:	\$19,100,813 *
		Less: Gain recognized on liquidation	\$18,016,371
		Previously Taxed Capital	\$1,084,442
III. Code Section 743(b) Adjustment based on Fair Market Value:			
	Fair Market Value less IRD	\$19,100,235	(\$19,100,813 -\$578) (Treas. Reg. Section 1.755-1(b)(4).)
	Less: Previously Taxed Capital	\$1,084,442	
	Section 743(b) Adjustment	\$18,015,793	(A)
IV. Code Section 743(b) Adjustment based on Estate Tax Audit:			
	Value of Membership Interest	\$17,815,000	
	Less: Income in respect of a Decedent	\$578	
	Tax basis of Membership Interest	\$17,814,422	
	Less: Trust's previously taxed capital	\$1,084,442	
	Section 743(b) Adjustment	\$16,729,980	(B)

* \$19,100,813 (liquidating proceeds) = \$20,609,423 (Fair Market Value of Company at date of death)*92.68% (Trust Percentage Interest)

Exhibit D

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	(A)	(B)	(C)	(D)
	Proportionate Share of	Tentative	Adjustment for	§ 755 Allocation
	<u>Tax Basis in Sasco's Assets</u>	<u>§ 755 Allocation</u>	<u>Negative Decrease*</u>	<u>((B)-(C))</u>
Real Estate	\$173,500.00	\$16,636,577.87	(\$6,249.83)	\$16,630,328.04
Sysco	0	\$24,663.64	(\$9.17)	\$24,654.47
Johnson & Johnson	0	(\$3,025.55)	\$3,025.55	\$0.00
Schering Plough	0	\$6,055.62	(\$2.25)	\$6,053.37
United Health Care	0	\$2,259.59	(\$0.84)	\$2,258.75
Cisco	0	(\$3,261.34)	\$3,261.34	\$0.00
Dover	0	\$7,246.37	(\$2.69)	\$7,243.68
Emerson	0	\$7,675.65	(\$2.85)	\$7,672.80
Berkshire Hathaway A	0	\$31,465.87	(\$11.70)	\$31,454.17
Berkshire Hathaway B	0	\$20,322.28	(\$7.56)	\$20,314.72
		\$16,729,980.00	\$0.00	\$16,729,980.00
<u>Column C: Treas. Reg. §1.755-1(b)(3)(iii)(B)</u>				
	(Column B Positive Adjustment)	x	\$6,286.89 (Total Value of Negative Adjustments)	
	(Total Column B Positive Adjustments of \$16,909,766.89)*			
	*\$16,909,766.89 = \$16,729,980 + \$6,286.89 + \$173,500			

Exhibit E

Examples 1 & 2 of Treas. Reg. § 1.755-1(b)(6): Sale of a Going Business

Sale of A's Interest to D for \$650,000 (ex. 1)

	<u>FMV</u>	<u>Gross Value</u>
Inventory	\$1,000,000	\$2,950,000 (aggregate value)
Building	2,000,000	
Intangible 1	50,000	0
Intangible 2	50,000	0
	<u>\$3,100,000</u>	<u>\$2,950,000</u>
Liability	1,000,000	1,000,000
A	\$700,000	\$650,000
B	700,000	650,000
C	700,000	650,000

Sale of A's interest for \$1,000,000 (ex. 2)

	<u>FMV</u>	<u>Gross Value</u>
Inventory	\$1,000,000	\$1,000,000
Building	2,000,000	2,000,000
Intangible 1	300,000	300,000
Intangible 2	300,000	300,000
Goodwill	0	400,000
	<u>\$3,600,000</u>	<u>\$4,000,000</u>
Liability	1,000,000	1,000,000
A	866,667	1,000,000
B	866,667	1,000,000
C	866,667	1,000,000