Section 736 - Payments to a Retiring Partner or Tax-Charts.com Start a Deceased Partner's Successor in Interest Copyright © 2011, Andrew Mitchel LLC Liq'n of Entire Dated July 27, 2011 Int. in P'ship N/A **Disclaimer** Vere payments made to a retiring partner or to a deceased partner's successor Section 736 does This flowchart has been extensively reviewed to be as in interest in liquidation of such partner's entire interest in the partnership? not apply. Reg. 1.736-1(a)(1)(i), Sec. 761(d), Reg. 1.761-1(d), Holman v. Commr 66 T.C. 809 (1976), affd, 564 F.2d 283 (9th Cir. 1977), Milliken v. Commr., 72 T.C. 256 (1979), aff'd in unpub. opin. (1st Cir. 1979) complete and accurate as possible. However, due to the Continue Yes Reg. 1.736 complexity of these rules, this flowchart undoubtedly includes 1(a)(1)(i) as Partner errors and omissions. You should consult a tax professional Did the estate or other successor in interest of a deceased for individual advice regarding your own situation. This partner continues as a partner in its own right under local law? flowchart is not updated for changes in the tax laws and Reg. 1.736-1(a)(1)(i) should not be relied upon for any purpose whatsoever. Pmts by P'ship **Treat as Distributive Share** Were payments made by the partnership The payments made in liquidation of the interest of the (rather than by the partners)? withdrawing partner are considered as a distributive share Reg. 1.736-1(a)(1)(i) to the recipient of partnership income. These payments 736(a) For P'ship With Regard to are taken into account under section 702 in the income of **Payments** Inc. of the P'ship the withdrawing partner and thus reduce the amount of **Property** the distributive shares of the remaining partners. The Were the payments made in exchange for the The payments Were the payments to payments are included in the income of the recipient for vithdrawing "partner's interest in partnership property" are treated as the withdrawing his taxable year with or within which ends the partnership Generally, the valuation placed by the partners ayments unde artner determined with taxable year for which the payment is a distributive share upon a partner's interest in partnership property in an section 736(a) regard to the income The withdrawing partner is regarded as a partner until arm's length agreement will be regarded as correct. If of the partnership? the entire interest of the withdrawing partner is liquidated. such valuation reflects only the partner's net interest in Sec. 736(a)(1) & (2) Reg. 1.736-1(a)(3) Sec. 736(a)(1), Reg. 1.736-1(a)(1)(ii), (a)(3), (4), (5), & (6) Rev. Rul. 75-154, Rev. Rul. 83-155 the property (i.e., total assets less liabilities), it must be adjusted so that both the value of the partner's interest in property and the basis for his interest take into Treat as Guaranteed Payments account the partner's share of partnership liabilities. Sec. 736(b)(1), Reg. 1.736-1(b)(1), Rev. Rul. 75-154, Wallis v. Commr., T.C. Memo. 2009-243, aff'd 11th Cir. 2010 The payments made in liquidation of the interest of the withdrawing partner are considered as a Quirk Est. v. Commr., 928 F. 2d 751 (6th Cir. 1991) Champlin v. Commr., T.C. Memo 1977-196 guaranteed payment described in section 707(c). These payments are deductible by the partnership Gen'l under section 162(a) and are taxable as ordinary Capital P'ship Unrealized Receivables Partner income to the recipient under section 61(a). Was the retiring or Was capital a Were the payments to the withdrawing partner for his/her The payments are included in the income of deceased partner material income interest in unrealized receivables of the partnership in the recipient for his taxable year in which the producing factor excess of their partnership basis, including any special partnership is entitled to deduct such amount as a general partner asis adjustment for them to which such partner is entitled? in the partnership? for the partnership? a guaranteed payment. The withdrawing partner is regarded as a partner until the entire interest Yes Sec. 736(b)(3)(B) Sec. 736(b)(3)(A) Sec. 736(b)(2)(A) No of the withdrawing partner is liquidated Reg. 1.736-1(b)(2) Rev. Rul. 75-154. Rev. Rul. 83-155 Stated Good Will No Apprec'd Good Will Vere the payments to the withdrawing partner for his/her interest Did the partnership agreement provide for a reasonable payment with in the partner's share of good will of the partnership espect to good will ("stated good will")? Generally, the valuation placed in excess of its partnership basis, including any special upon good will by an arm's length agreement of the partners, whether basis adjustments for it to which such partner is entitled? specific in amount or determined by a formula, is regarded as correct Sec. 736(b)(2)(B), Reg. 1.736-1(b)(3), Smith v. Commr., 37 T.C. 1033 (1962), affd, 313 F.2d 16 (10th Cir. 1962) Commr. v. Jackson Investment Co., 346 F.2d 187 (9th Cir. 1965) Sec. 736(b)(2)(B) 736(b) **Payments** Spector v. Commr., 641 F.2d 376 (5th Cir 1981) Jacobs v. Commr., T.C. Memo 1974-196 are considered as made in exchange for such partner's interest in partnership property and are treated as payments under section 736(b). Reg. 1.736-1(b)(4) 751(b) May Apply Inventory Were the payments to the Payments for an interest in substantially appreciated inventory items, as defined in section 751(d), are subject to the rules provided in section 751(b) and Reg. 1.751-1(b). The partnership basis in inventory items as to a deceased partner's successor in interest does not change be withdrawing partner for his/her interest in inventory? of the death of the partner unless the partnership has elected the optional basis adjustment under section 754. But see Reg. 1.751-1(b)(3)(iii). Reg. 1.736-1(b)(4) Reg. 1.736-1(b)(4) Lig'n Distrib'n The payments are considered as a distribution by the partnership in complete liquidation under sections 731, 732, and where applicable, 751. The payments are taken into account by the recipient for his/her taxable year in which such payments are made. The withdrawing partner is regarded as a partner until the entire interest of the withdrawing partner is liquidated. Sec. 736(b), Reg. 1.736-1(a)(2), (5) & (6) Annual **Fixed Amount Fixed Years Pro Rata Allocation** Payments 🗼 Agreed Upon Allocation The preceding boxes determined Have all the remaining partners and the Was a fixed amount (whether or not Allocate each fixed agreed payment the portion of the total section 736 withdrawing partner or his/her successor supplemented by any additional amounts) to pro rata between section 736(a) and payments that will be considered in interest agreed to an allocation of each be received over a fixed number of years? 736(b) in the same ratio as all fixed section 736(a) payments and 736(b) annual payment between section 736(a) agreed payments for the fixed Reg. 1.736-1(b)(5)(i) and (b), provided that the total amount payments. However, typically section number of years are treated as 736 payments are made to the allocated to property under section ection 736(a) and 736(b) payments 736(b) First 736(b) does not exceed the fair market If the amount received in a year is withdrawing partner over multiple years. Consequently, the payments value of such property at the ess than the fixed agreed payments The payments received by the retiring received in each year must be date of death or retirement? partner or deceased partner's successor for that year, a special "catch-up" rule accelerates the section allocated between section 736(a) in interest are first treated as payments in Yes Reg. 1.736-1(b)(5)(iii) and section 736(b). The following exchange for his/her interest in partnership 736(b) portion in future years Alloc. As Agreed boxes determine how the annual roperty under section 736(b) to the extent of Reg. 1.736-1(b)(5)(i) allocation between section 736(a) the value of that interest and, thereafter, Allocate each annual payment between and section 736(b) should be made as payments under section 736(a). section 736(a) and (b) as agreed Reg. 1.736-1(b)(5) Reg. 1.736-1(b)(5)(ii) Reg. 1.736-1(b)(5)(iii) 736(b) Pmts **Fixed Sum** Proportionate Gain Election Has the retiring partner or a deceased partner's successor in interest elected (in his/her tax return for the first taxable year for which he/she Were the total of section 736(b) Yes receives such payments), to report and to measure the amount of any gain or loss by the difference between (i) the amount treated as a distribution under section 736(b) in that year, and (ii) the portion of the adjusted basis of the partner for his partnership interest attributable payments a fixed sum? Reg. 1.736-1(b)(6) to such distribution (i.e., the amount which bears the same proportion to the partner's total adjusted basis for his partnership interest as **Basis First** the amount distributed under section 736(b) in that year bears to the total amount to be distributed under section 736(b))? Reg. 1.736-1(b)(6) Gains or Loss with respect to section Alloc. Gain 736(b) payments are determined under section 731 (generally no gain Proportionately Allocate gain related to section 736(b) payments until distributions exceed basis). tween the years as described in the preceding box.

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