PROPOSALS WOULD TAX PARTNERSHIP INTERESTS TRANSFERRED FOR SERVICES UNDER RESTRICTED PROPERTY RULES

The IRS has issued proposed regulations which would apply the restricted property rules of Code Sec. 83 to determine the tax consequences of a partnership's transfer of either a capital or profits interest in exchange for services. The IRS also has issued a Notice carrying a proposed revenue procedure fleshing out a safe harbor which would be included in the regulations for determining the value of a transferred interest.

■ Highlights of the proposed regulations

The proposed regulations would adopt the following approach for taxing partnership interests transferred in exchange for services:

- A partnership capital or profits interest would be property under Code Sec. 83 , and the transfer of a partnership interest in connection with the performance of services would be subject to Code Sec. 83 .

- A transferee would be treated as a partner for income tax purposes if a Code Sec. 83 (b) election is made; if such an election is not made, then the holder of the partnership interest would not be treated as a partner until the interest becomes substantially vested.

- The timing and amount of the partnership's compensation deduction would be governed by Code Sec. 83.

- The amount includible by the transferee and deductible by the partnership generally would equal the fair market value of the transferred interest.

- Because partnership interests can be difficult to value, and to help partnerships maintain capital accounts properly, a partnership and its partners would be allowed to elect a safe harbor under which the fair market value of a partnership interest would be treated as equal to the liquidation value of the interest. The related Notice includes a draft revenue procedure describing additional rules and conditions relating to the safe harbor election.

- A partnership transferring a partnership interest in exchange for services generally would recognize no gain or loss on the transfer.

- The service provider's capital account would be increased by the amount he takes into income as a result of receiving the interest, plus any amounts paid for it.