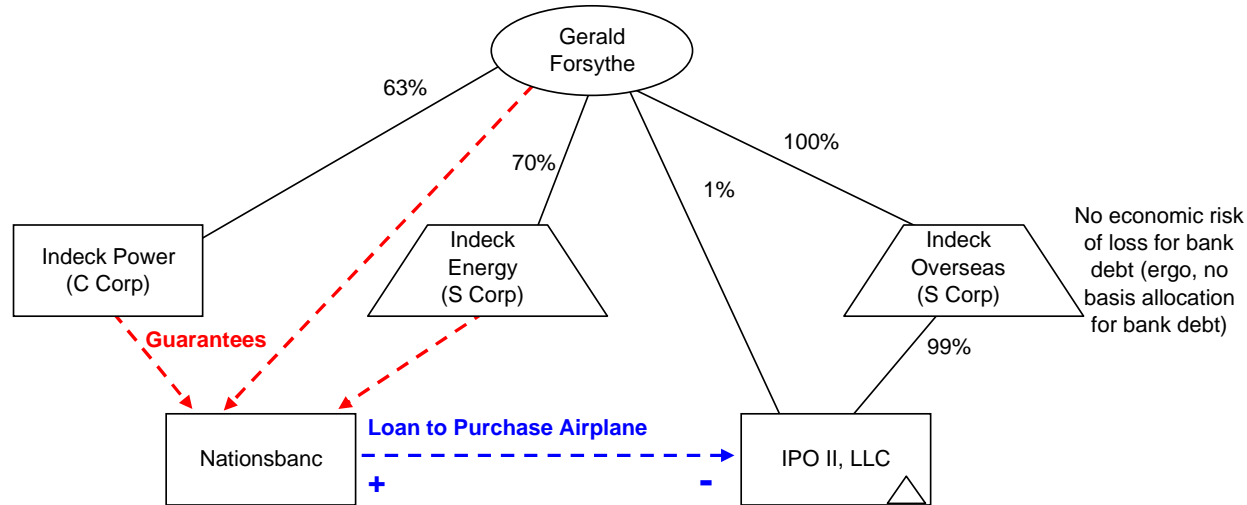


**Forsythe v. Commissioner
122 T.C. 295 (2004)**

**Special Allocation Allowed Only
to the Extent of EROL**

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△ Means "flow-thru" for U.S. tax purposes

IPO II was treated as a partnership for Federal income tax purposes. The members of IPO II were Mr. Forsythe and Indeck Overseas. Indeck Overseas was an S corporation in which Mr. Forsythe owned 100% of the outstanding shares. The members' interests in the profits and losses of IPO II were allocated as follows: Indeck Overseas, 99 units; Mr. Forsythe, 1 unit. Mr. Forsythe also owned 70% of the outstanding shares of Indeck Energy Services, Inc. (Indeck Energy). Indeck Energy elected to be treated as an S corporation. Mr. Forsythe also owned 63% of the outstanding shares of Indeck Power Equipment Co. (Indeck Power), a C corporation.

IPO II purchased an aircraft and two engines for a total purchase price of \$9,406,175, which was funded by a loan from Nationsbank. Indeck Energy, Indeck Power, and Mr. Forsythe guaranteed the loan. The IRS determined that 100% of the recourse liability was allocable to Mr. Forsythe and none of the liability was allocable to Indeck Overseas.

A partner's distributive share of partnership loss is allowed only to the extent of the adjusted basis of the partner's interest in the partnership at the end of the partnership year in which the loss occurred. Sec. 704(d). Any increase in a partner's share of liabilities of the partnership is considered a contribution by such partner to the partnership, and, consequently, increases the basis of the partner's interest in the partnership. Sec. 752(a). Reg. 1.752-1(a)(1) defines a partnership liability as a recourse liability "to the extent that any partner or related person bears the economic risk of loss ("EROL") for that liability under §1.752-2." Reg. 1.752-2 provides the test for determining whether a partner or related person bears the economic risk of loss. The determination to be made is whether, if the partnership were constructively liquidated, the partner or related person would be obligated to make a payment when the liability became due and payable. Reg. 1.752-2(b)(1).

The court held that in a constructive liquidation Indeck Overseas would not directly bear the economic risk of loss for the Nationsbank loan. Further, the related partner exception of Reg. 1.752-4(b)(2)(iii) did not apply. Consequently, the entire recourse liability incurred with the purchase of the aircraft was allocable to Mr. Forsythe.

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