



# Instructions for Form 1065

## U.S. Return of Partnership Income

Section references are to the Internal Revenue Code unless otherwise noted.

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### Changes To Note

- Additional guidance has been issued allowing qualifying small businesses to use the cash method of accounting. For details, see Rev. Proc. 2002-28, 2002-18, I.R.B. 815. Also see **Cost of Goods Sold** on page 19.
- As a result of changes to the North American Industry Classification System, some of the codes for Principal Business Activities have changed beginning in 2002. These changes have mainly occurred in the Construction, Wholesale Trade, and Information sectors. See pages 33 through 35 for the new applicable codes that should be entered in item C of page 1 of Form 1065.
- For tax years ending on or after December 31, 2001, if the partnership must make a section 481(a) adjustment because of an accounting method change, the adjustment period for a negative adjustment is now 1 year. For details, including special rules and exceptions, see Rev. Proc. 2002-19, 2002-13 I.R.B. 696 as amplified and clarified by Rev. Proc. 2002-54, 2002-35 I.R.B. 432, and **Change in accounting method** on page 5.

- Additional guidance was issued regarding the procedures under which a taxpayer may obtain automatic consent of the Commissioner to change certain methods of accounting. See Rev. Proc. 2002-9, 2002-3 I.R.B. 327, as modified and clarified by Rev. Proc. 2002-19 and 2002-54.
- The partnership must file a disclosure statement for each reportable tax shelter transaction in which it participated, directly or indirectly, if the transaction is reasonably expected to affect any partner's Federal income tax liability. See **Tax Shelter Disclosure Statement** on page 8 for more details.

### Photographs of Missing Children

The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in instructions on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1-800-THE-LOST** (1-800-843-5678) if you recognize a child.

### Unresolved Tax Issues

If the partnership has attempted to deal with an IRS problem unsuccessfully, it should contact the Taxpayer Advocate. The Taxpayer Advocate independently represents the partnership's interests and concerns within the IRS by protecting its rights and resolving problems that have not been fixed through normal channels.

While the Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that the partnership's case is given a complete and impartial review.

The partnership's assigned personal advocate will listen to its point of view and will work with the partnership to address its concerns. The partnership can expect the advocate to provide:

- A "fresh look" at a new or on-going problem.
- Timely acknowledgement.
- The name and phone number of the individual assigned to its case.
- Updates on progress.
- Timeframes for action.
- Speedy resolution.
- Courteous service.

When contacting the Taxpayer Advocate, the partnership should provide the following information:

- The partnership's name, address, and employer identification number.
- The name and telephone number of an authorized contact person and the hours he or she can be reached.
- The type of tax return and year(s) involved.
- A detailed description of the problem.
- Previous attempts to solve the problem and the office that had been contacted.
- A description of the hardship the partnership is facing (if applicable).

The partnership may contact a Taxpayer Advocate by calling a toll-free number, **1-877-777-4778**. Persons who have access to TTY/TDD equipment may call 1-800-829-4059 and ask for the Taxpayer Advocate. If the partnership prefers, it may call, write, or fax the Taxpayer Advocate office in its area. See **Pub. 1546**, The Taxpayer Advocate Service of the IRS, for a list of addresses and fax numbers.

## How To Get Forms and Publications

### Personal Computer

You can access the IRS Web Site 24 hours a day, 7 days a week at **www.irs.gov** to:

- Order IRS products on-line.
- Download forms, instructions, and publications.
- See answers to frequently asked tax questions.
- Search publications on-line by topic or keyword.
- Send us comments or request help by e-mail.
- Sign up to receive local and national tax news by e-mail.

You can also reach us using file transfer protocol at **ftp.irs.gov**.

### CD-ROM

Order **Pub. 1796**, 2002 Federal Tax Products CD-ROM, and get:

- Current year forms, instructions, and publications.
- Prior year forms, instructions, and publications.
- Frequently requested tax forms that may be filled in electronically, printed out for submission, and saved for recordkeeping.
- The Internal Revenue Bulletin.

Buy the CD-ROM on the Internet at **www.irs.gov/cdorders** from the National Technical Information Service (NTIS) for \$22 (no handling fee), or call **1-877-CDFORMS** (1-877-233-6767) toll free to buy the CD-ROM for \$22 (plus a \$5 handling fee).

### By Phone and In Person

You can order forms and publications 24 hours a day, 7 days a week, by calling **1-800-TAX-FORM** (1-800-829-3676). You can also get most forms and publications at your local IRS office.

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## General Instructions

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### Purpose of Form

Form 1065 is an information return used to report the income, deductions, gains, losses, etc., from the operation of a partnership. A partnership does not pay tax on its income but "passes through" any profits or losses to its partners. Partners must include partnership items on their tax returns.

### Definitions

#### Partnership

A partnership is the relationship between two or more persons who join to carry on a trade or business, with each person contributing money, property, labor, or skill and each expecting to share in the profits and losses of the business whether or not a formal partnership agreement is made.

The term "partnership" includes a limited partnership, syndicate, group, pool, joint venture, or other unincorporated organization, through or by which any business, financial operation, or venture is carried on, that is not, within the meaning of the regulations under section 7701, a corporation, trust, estate, or sole proprietorship.

A joint undertaking merely to share expenses is not a partnership. Mere co-ownership of property that is maintained and leased or rented is not a partnership. However, if the co-owners provide services to the tenants, a partnership exists.

#### Foreign Partnership

A foreign partnership is a partnership that is not created or organized in the United States or under the law of the United States or of any state.

#### General Partner

A general partner is a partner who is personally liable for partnership debts.

#### General Partnership

A general partnership is composed only of general partners.

#### Limited Partner

A limited partner is a partner in a partnership formed under a state limited partnership law, whose personal liability for partnership debts is limited to the amount of money or other property that the partner contributed or is required to contribute to the partnership. Some members of other entities, such as domestic or foreign business trusts or limited liability companies that are classified as partnerships, may be treated as limited partners for certain purposes. See, for example, Temporary Regulations section 1.469-5T(e)(3), which treats all members with limited liability as limited partners for purposes of section 469(h)(2).

### Limited Partnership

A limited partnership is formed under a state limited partnership law and composed of at least one general partner and one or more limited partners.

### Limited Liability Partnership

A limited liability partnership (LLP) is formed under a state limited liability partnership law. Generally, a partner in an LLP is not personally liable for the debts of the LLP or any other partner, nor is a partner liable for the acts or omissions of any other partner, solely by reason of being a partner.

### Limited Liability Company

A limited liability company (LLC) is an entity formed under state law by filing articles of organization as an LLC. Unlike a partnership, none of the members of an LLC are personally liable for its debts. An LLC may be classified for Federal income tax purposes either as a partnership, a corporation, or an entity disregarded as an entity separate from its owner by applying the rules in Regulations section 301.7701-3. See **Form 8832**, Entity Classification Election, for more details.

**Note:** A domestic LLC with at least two members that does not file Form 8832 is classified as a partnership for Federal income tax purposes.

### Nonrecourse Loans

Nonrecourse loans are those liabilities of the partnership for which no partner bears the economic risk of loss.

### Who Must File

#### Domestic Partnerships

Except as provided below, every domestic partnership must file Form 1065, unless it neither receives income nor incurs any expenditures treated as deductions or credits for Federal income tax purposes.

Entities formed as LLCs that are classified as partnerships for Federal income tax purposes must file Form 1065.

A religious or apostolic organization exempt from income tax under section 501(d) must file Form 1065 to report its taxable income, which must be allocated to its members as a dividend, whether distributed or not. Such an organization must figure its taxable income on an attachment to Form 1065 in the same manner as a corporation. The organization may use **Form 1120**, U.S. Corporation Income Tax Return, for this purpose. Enter the organization's taxable income, if any, on line 4b of Schedule K and each member's pro rata share on line 4b of Schedule K-1. Net operating losses are not deductible by the members but may be carried back or forward by the organization under the rules of section 172. The religious or apostolic organization also must make its annual information return available for public inspection. For this purpose, "annual information return" includes an exact copy of Form 1065 and all accompanying

schedules and attachments, except Schedules K-1. For more details, see Regulations section 301.6104(d)-3.

A qualifying syndicate, pool, joint venture, or similar organization may elect under section 761(a) not to be treated as a partnership for Federal income tax purposes and will not be required to file Form 1065 except for the year of election. For details, see section 761(a) and Regulations section 1.761-2.

An electing large partnership (as defined in section 775) must file **Form 1065-B**, U.S. Return of Income for Electing Large Partnerships.

Real estate mortgage investment conduits (REMICs) must file **Form 1066**, U.S. Real Estate Mortgage Investment Conduit (REMIC) Income Tax Return.

Certain publicly traded partnerships treated as corporations under section 7704 must file Form 1120.

## Foreign Partnerships

Generally, a foreign partnership that has gross income effectively connected with the conduct of a trade or business within the United States or has gross income derived from sources in the United States must file Form 1065, even if its principal place of business is outside the United States or all its members are foreign persons. A foreign partnership required to file a return generally must report all of its foreign and U.S. source income.

A foreign partnership with U.S. source income is not required to file Form 1065 if it qualifies for either of the following two exceptions.

**Exception for foreign partnerships with U.S. partners.** A return is not required if:

- The partnership had no effectively connected income (ECI) during its tax year,
- The partnership had U.S. source income of \$20,000 or less during its tax year,
- Less than 1% of any partnership item of income, gain, loss, deduction, or credit was allocable in the aggregate to direct U.S. partners at any time during its tax year, **and**
- The partnership is not a withholding foreign partnership as defined in Regulations section 1.1441-5(c)(2)(i).

**Exception for foreign partnerships with no U.S. partners.** A return is not required if:

- The partnership had no ECI during its tax year,
- The partnership had no U.S. partners at any time during its tax year,
- All required Forms 1042 and 1042-S were filed by the partnership or another withholding agent as required by Regulations section 1.1461-1(b) and (c),
- The tax liability of each partner for amounts reportable under Regulations sections 1.1461-1(b) and (c) has been fully satisfied by the withholding of tax at the source, **and**

- The partnership is not a withholding foreign partnership as defined in Regulations section 1.1441-5(c)(2)(i).

A foreign partnership filing Form 1065 solely to make an election (such as an election to amortize organization expenses) need only provide its name, address, and employer identification number (EIN) on page one of the form and attach a statement citing “Regulations section 1.6031(a)-1(b)(5)” and identifying the election being made. A foreign partnership filing Form 1065 solely to make an election must obtain an EIN if it does not already have one.

## Termination of the Partnership

A partnership terminates when:

1. All its operations are discontinued and no part of any business, financial operation, or venture is continued by any of its partners in a partnership **or**
2. At least 50% of the total interest in partnership capital and profits is sold or exchanged within a 12-month period, including a sale or exchange to another partner. See Regulations section 1.708-1(b)(1) for more details.

The partnership’s tax year ends on the date of termination. For purposes of **1** above, the date of termination is the date the partnership winds up its affairs. For purposes of **2** above, the date of termination is the date the partnership interest is sold or exchanged that, of itself or together with other sales or exchanges in the preceding 12 months, transfers an interest of 50% or more in both partnership capital and profits.

Special rules apply in the case of a merger, consolidation, or division of a partnership. See Regulations sections 1.708-1(c) and (d) for details.

## Electronic Filing

Certain partnerships with more than 100 partners are required to file Form 1065, Schedules K-1, and related forms and schedules electronically. Other partnerships generally have the option to file electronically. Unless otherwise noted, this requirement or option does not apply to:

- Partnership returns with a foreign address on Form 1065.
- Fiscal year returns with a tax period ending after June 30, 2003. Partnerships with any other fiscal year returns ending on or before June 30, 2003 (January 2003–June 2003) may voluntarily file their return electronically.

**Note:** *Fiscal year returns with an extended due date after October 15, 2003, may not file electronically.*

- Returns filed for religious or apostolic organizations under section 501(d)(3) or for organizations electing not to be treated as a partnership under section 761(a).
- Common trust fund returns. Common trust funds using Form 1065 to make a

return of income may voluntarily file Form 1065 electronically.

- Returns filed on Form 1065-B.

## For more details on electronic filing, see:

- **Pub. 1524**, Procedures for the 1065 e-file Program, U.S. Return of Partnership Income For Tax Year 2002;
- **Pub. 1525**, File Specifications, Validation Criteria and Record Layouts for the 1065 e-file Program, U.S. Return of Partnership Income for Tax Year 2002;
- **Pub. 3416**, 1065 e-file Program, U.S. Return of Partnership Income for Tax Year 2002 (Publication 1525 Supplement);
- **Pub. 3225**, Test Package for Electronic Filers of U.S. Return of Partnership Income for Tax Year 2002;
- **Form 9041**, Application/Registration for Electronic/Magnetic Media Filing of Business Returns; and
- **Form 8453-P**, U.S. Partnership Declaration and Signature for Electronic Filing.

## For more information on filing electronically:

- **Call** the Electronic Filing Section at the Ogden Service Center at 801-620-7444 (not a toll-free call) or
- **Write** to Internal Revenue Service, Ogden Submission Processing Center (OSPC), 1973 N. Rulon White Blvd., Stop 1056, Ogden, UT 84201.

## Electronic Filing Waiver

The IRS may waive the electronic filing rules if the partnership demonstrates that a hardship would result if it were required to file its return electronically. A partnership interested in requesting a waiver of the mandatory electronic filing requirement must file a written request, and request one in the manner prescribed by the Ogden Submission Processing Center (OSPC).

- All written requests for waivers should be mailed to:  
Internal Revenue Service  
Ogden Submission Processing Center  
1973 N. Rulon White Blvd., Stop 1057  
Ogden, UT 84201
- Contact OSPC at (801) 620-7444 for questions regarding the waiver procedures or process.

## When To File

Generally, a domestic partnership must file Form 1065 by the 15th day of the 4th month following the date its tax year ended as shown at the top of Form 1065. For partnerships that keep their records and books of account outside the United States and Puerto Rico, an extension of time to file and pay is granted to the 15th day of the 6th month following the close of the tax year. If the due date falls on a Saturday, Sunday, or legal holiday, file by the next business day.



## Private Delivery Services

The partnership can use certain private delivery services designated by the IRS to meet the "timely mailing as timely filing/paying" rule for Form 1065. The most recent list of designated private delivery services was published by the IRS in September 2002. The list includes only the following:

- Airborne Express (Airborne): Overnight Air Express Service, Next Afternoon Service, Second Day Service.
- DHL Worldwide Express (DHL): DHL "Same Day" Service, DHL USA Overnight.
- Federal Express (FedEx): FedEx Priority Overnight, FedEx Standard Overnight, FedEx 2Day, FedEx International Priority, and FedEx International First.
- United Parcel Service (UPS): UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, UPS 2nd Day Air A.M., UPS Worldwide Express Plus, and UPS Worldwide Express.

The private delivery service can tell you how to get written proof of the mailing date.

## Extension

If you need more time to file a partnership return, file **Form 8736**, Application for Automatic Extension of Time To File U.S. Return for a Partnership, REMIC, or for Certain Trusts, for an automatic 3-month extension. File Form 8736 by the regular due date of the partnership return. The automatic 3-month extension period

includes any 2-month extension granted to partnerships that keep their records and books of account outside the United States and Puerto Rico.

If, after you have filed Form 8736, you still need more time to file the partnership return, file **Form 8800**, Application for Additional Extension of Time To File U.S. Return for a Partnership, REMIC, or for Certain Trusts, for an additional extension of up to 3 months. The partnership must provide a full explanation of the reasons for requesting the extension in order to get this additional extension. Form 8800 must be filed by the extended due date of the partnership return.

## Period Covered

Form 1065 is an information return for calendar year 2002 and fiscal years beginning in 2002 and ending in 2003. If the return is for a fiscal year or a short tax year, fill in the tax year space at the top of the form.

The 2002 Form 1065 may also be used if:

1. The partnership has a tax year of less than 12 months that begins and ends in 2003 and
2. The 2003 Form 1065 is not available by the time the partnership is required to file its return.

However, the partnership must show its 2003 tax year on the 2002 Form 1065 and incorporate any tax law changes that are effective for tax years beginning after 2002.

## Who Must Sign

### General Partner or LLC Member

Form 1065 is not considered to be a return unless it is signed. One general partner or LLC member must sign the return. If a receiver, trustee in bankruptcy, or assignee controls the organization's property or business, that person must sign the return.

### Paid Preparer's Information

If a partner or an employee of the partnership completes Form 1065, the paid preparer's space should remain blank. In addition, anyone who prepares Form 1065 but does not charge the partnership should not complete this section.

Generally, anyone who is paid to prepare the partnership return **must**:

- Sign the return, by hand, in the space provided for the preparer's signature. Signature stamps or labels are not acceptable.
- Fill in the other blanks in the **Paid Preparer's Use Only** area of the return.
- Give the partnership a copy of the return in addition to the copy to be filed with the IRS.

### Paid Preparer Authorization

If the partnership wants to allow the paid preparer to discuss its 2002 Form 1065 with the IRS, check the "Yes" box in the signature area of the return. The authorization applies only to the individual whose signature appears in the "Paid Preparer's Use Only" section of its return. It does not apply to the firm, if any, shown in the section.

If the "Yes" box is checked, the partnership is authorizing the IRS to call the paid preparer to answer any questions that may arise during the processing of its return. The partnership is also authorizing the paid preparer to:

- Give the IRS any information that is missing from its return,
- Call the IRS for information about the processing of its return, and
- Respond to certain IRS notices that the partnership has shared with the preparer about math errors and return preparation. The notices will not be sent to the preparer.

The partnership is not authorizing the paid preparer to bind the partnership to anything or otherwise represent the partnership before the IRS. If the partnership wants to expand the paid preparer's authorization, see **Pub. 947**, Practice Before the IRS and Power of Attorney.

The authorization cannot be revoked. However, the authorization will automatically end no later than the due date (excluding extensions) for filing the 2003 return.

## Where To File

File Form 1065 at the applicable IRS address listed below.

If the partnership's principal business, office, or agency is located in:	And the total assets at the end of the tax year (Form 1065, page 1, item F) are:	Use the following Internal Revenue Service Center address:
Connecticut, Delaware, District of Columbia, Illinois, Indiana, Kentucky, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, West Virginia, Wisconsin	Less than \$10 million	Cincinnati, OH 45999-0011
	\$10 million or more	Ogden, UT 84201-0011
Alabama, Alaska, Arizona, Arkansas, California, Colorado, Florida, Georgia, Hawaii, Idaho, Iowa, Kansas, Louisiana, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Tennessee, Texas, Utah, Washington, Wyoming	Any amount	Ogden, UT 84201-0011
A foreign country or U.S. possession	Any amount	Philadelphia, PA 19255-0011

## Penalties

### Late Filing of Return

A penalty is assessed against the partnership if it is required to file a partnership return and it **(a)** fails to file the return by the due date, including extensions, or **(b)** files a return that fails to show all the information required, unless such failure is due to reasonable cause. If the failure is due to reasonable cause, attach an explanation to the partnership return. The penalty is \$50 for each month or part of a month (for a maximum of 5 months) the failure continues, multiplied by the total number of persons who were partners in the partnership during any part of the partnership's tax year for which the return is due. This penalty will not be imposed on partnerships for which the answer to Question 4 on Schedule B of Form 1065 is **No**, provided all partners have timely filed income tax returns fully reporting their shares of the income, deductions, and credits of the partnership. See page 20 of the instructions for further information.

### Failure To Furnish Information Timely

For each failure to furnish Schedule K-1 to a partner when due and each failure to include on Schedule K-1 all the information required to be shown (or the inclusion of incorrect information), a \$50 penalty may be imposed with respect to each Schedule K-1 for which a failure occurs. The maximum penalty is \$100,000 for all such failures during a calendar year. If the requirement to report correct information is intentionally disregarded, each \$50 penalty is increased to \$100 or, if greater, 10% of the aggregate amount of items required to be reported, and the \$100,000 maximum does not apply.

### Trust Fund Recovery Penalty

This penalty may apply if certain excise, income, social security, and Medicare taxes that must be collected or withheld are not collected or withheld, or these taxes are not paid. These taxes are generally reported on:

- **Form 720**, Quarterly Federal Excise Tax Return;
- **Form 941**, Employer's Quarterly Federal Tax Return;
- **Form 943**, Employer's Annual Tax Return for Agricultural Employees; or
- **Form 945**, Annual Return of Withheld Federal Income Tax.

The trust fund recovery penalty may be imposed on all persons who are determined by the IRS to have been **responsible** for collecting, accounting for, and paying over these taxes, and who acted willfully in not doing so. The penalty is equal to the unpaid trust fund tax. See the Instructions for Form 720, **Pub. 15**, Circular E, Employer's Tax Guide, or **Pub. 51**, Circular A, Agricultural Employer's Tax Guide, for more details,

including the definition of a responsible person.

## Accounting Methods

Figure ordinary income using the method of accounting regularly used in keeping the partnership's books and records.

Generally, permissible methods include:

- Cash,
- Accrual, or
- Any other method authorized by the Internal Revenue Code.

In all cases, the method used must clearly reflect income.

Generally, a partnership may not use the cash method of accounting if **(a)** it has at least one corporate partner, average annual gross receipts of more than \$5 million, and it is not a farming business or **(b)** it is a tax shelter (as defined in section 448(d)(3)). See section 448 for details. If inventories are required, the accrual method must be used for sales and purchases of merchandise. However, qualifying taxpayers and eligible businesses of qualifying small business taxpayers are excepted from using the accrual method and may account for inventoriable items as materials and supplies that are not incidental. For more details, see **Schedule A—Cost of Goods Sold**, on page 19.

**Accrual method.** Under the accrual method, an amount is includible in income when:

- All the events have occurred that fix the right to receive the income which is the earliest of the date: **(a)** the required performance takes place, **(b)** payment is due, or **(c)** payment is received, and
- The amount can be determined with reasonable accuracy.

See Regulations section 1.451-1(a) for details.

Generally, an accrual basis taxpayer can deduct accrued expenses in the tax year in which:

- All events that determine liability have occurred,
- The amount of the liability can be figured with reasonable accuracy, and
- Economic performance takes place with respect to the expense.

There are exceptions to the economic performance rule for certain items, including recurring expenses. See section 461(h) and the related regulations for the rules for determining when economic performance takes place.

### Nonaccrual experience method.

Accrual method partnerships are not required to accrue certain amounts to be received from the performance of services that, on the basis of their experience, will not be collected, if:

- The services are in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting or
- The partnership's average annual gross receipts for the 3 prior tax years does not exceed \$5 million.

This provision does not apply to any amount if interest is required to be paid

on the amount or if there is any penalty for failure to timely pay the amount. For information, see Chapter 11 of **Pub. 535**, Business Expenses.

### Percentage of completion method.

Long-term contracts (except for certain real property construction contracts) must generally be accounted for using the percentage of completion method described in section 460. See section 460 and the underlying regulations for rules on long-term contracts.

### Mark-to-market accounting method.

Dealers in securities must use the "mark-to-market" accounting method described in section 475. Under this method, any security that is inventory to the dealer must be included in inventory at its fair market value (FMV). Any security that is not inventory and that is held at the close of the tax year is treated as sold at its FMV on the last business day of the tax year, and any gain or loss must be taken into account in determining gross income. The gain or loss taken into account is generally treated as ordinary gain or loss. For details, including exceptions, see section 475 and the related regulations.

### Dealers in commodities and traders in securities and commodities

may elect to use the mark-to-market accounting method. To make the election, the partnership must file a statement describing the election, the first tax year the election is to be effective, and, in the case of an election for traders in securities or commodities, the trade or business for which the election is made. Except for new taxpayers, the statement must be filed by the due date (not including extensions) of the income tax return for the tax year immediately **preceding** the election year and attached to that return, or, if applicable, to a request for an extension of time to file that return. For more details, see Rev. Proc. 99-17, 1999-1 C.B. 503, and sections 475(e) and (f).

### Change in accounting method.

Generally, the partnership must get IRS consent to change its method of accounting used to report income (for income as a whole or for any material item). To do so, it must file **Form 3115**, Application for Change in Accounting Method. However, there are new procedures under which a partnership may obtain automatic consent to certain changes in accounting method. See Rev. Proc. 2002-9, 2002-3 I.R.B. 327 as modified by Rev. Proc. 2002-19, 2002-13 I.R.B. 696 and Rev. Proc. 2002-54, 2002-35 I.R.B. 432. For more information, see Form 3115 and **Pub. 538**, Accounting Periods and Methods.

Certain partnerships that are qualifying taxpayers or small business taxpayers that want to use the cash method for an eligible trade or business (described on page 19) may get an automatic consent to change their method of accounting. For details, see Rev. Proc. 2001-10, 2001-2

I.R.B. 272, Rev. Proc. 2002-28 and Form 3115.

**Example.** The partnership changes to the cash method of accounting. It accrued sales in 2001 for which it received payment in 2002. It must report those sales in both years as a result of changing its accounting method and must make a section 481(a) adjustment to prevent duplication of income.

**Section 481(a) adjustment.** The partnership may have to make an adjustment to prevent amounts of income or expenses from being duplicated. This is called a section 481(a) adjustment. The section 481(a) adjustment period is generally 1 year for a net negative adjustment and 4 years for a net positive adjustment. However, a partnership may elect to use a 1-year adjustment period if the net section 481(a) adjustment for the change is less than \$25,000. The partnership must complete the appropriate lines of Form 3115 to make the election. For more details on the section 481(a) adjustment, see Rev. Proc. 2002-19 as amplified and clarified by Rev. Proc. 2002-54.

Include any net positive section 481(a) adjustment on page 1, line 7. If the net section 481(a) adjustment is negative, report it on Form 1065, line 20.

## Accounting Periods

A partnership is generally required to have one of the following tax years:

1. The tax year of a majority of its partners (majority tax year).
2. If there is no majority tax year, then the tax year common to all of the partnership's principal partners (partners with an interest of 5% or more in the partnership profits or capital).
3. If there is neither a majority tax year nor a tax year common to all principal partners, then the tax year that results in the least aggregate deferral of income.

**Note:** *In determining the tax year of a partnership under 1, 2, or 3 above, the tax years of certain tax-exempt and foreign partners are disregarded. See Regulations section 1.706-1(b) for more details.*

4. Some other tax year, if:
  - The partnership can establish that there is a business purpose for the tax year (see Rev. Proc. 2002-39, 2002-22 I.R.B.1046); or
  - The partnership satisfies the 25% gross receipts test for a natural business year other than its required tax year (see Rev. Proc. 2002-38, 2002-2 I.R.B. 1037); or
  - The tax year is a "grandfathered" year (see Rev. Proc. 2002-38); or
  - The partnership elects under section 444 to have a tax year other than a required tax year by filing **Form 8716**, Election to Have a Tax Year Other Than a Required Tax Year. For a partnership to have this election in effect, it must make the payments required by section 7519

and file **Form 8752**, Required Payment or Refund Under Section 7519.

A section 444 election ends if a partnership changes its accounting period to its required tax year or some other permitted year or it is penalized for willfully failing to comply with the requirements of section 7519. If the termination results in a short tax year, type or legibly print at the top of the first page of Form 1065 for the short tax year, "SECTION 444 ELECTION TERMINATED."

To change an accounting period, see Pub. 538 and **Form 1128**, Application To Adopt, Change, or Retain a Tax Year, (unless the partnership is making an election under section 444).

**Note:** *The tax year of a common trust fund must be the calendar year.*

## Rounding Off to Whole Dollars

You may round off cents to whole dollars on your return and accompanying schedules. To do so, drop amounts under 50 cents and increase amounts from 50 to 99 cents to the next higher dollar.

## Recordkeeping

The partnership must keep its records as long as they may be needed for the administration of any provision of the Internal Revenue Code. If the consolidated audit procedures of sections 6221 through 6233 apply, the partnership usually must keep records that support an item of income, deduction, or credit on the partnership return for 3 years from the date the return is due or is filed, whichever is later. If the consolidated audit procedures do not apply, these records usually must be kept for 3 years from the date each partner's return is due or is filed, whichever is later. Keep records that verify the partnership's basis in property for as long as they are needed to figure the basis of the original or replacement property.

The partnership should also keep copies of all returns it has filed. They help in preparing future returns and in making computations when filing an amended return.

## Amended Return

To correct an error on a Form 1065 already filed, file an amended Form 1065 and check box G(5) on page 1. If the income, deductions, credits, or other information provided to any partner on Schedule K-1 are incorrect, file an amended Schedule K-1 (Form 1065) for that partner with the amended Form 1065. Also give a copy of the amended Schedule K-1 to that partner. Check box I(2) on the Schedule K-1 to indicate that it is an amended Schedule K-1.

**Exception:** *If you are filing an amended partnership return and you answered Yes to Question 4 in Schedule B, the tax matters partner must file **Form 8082**, Notice of Inconsistent Treatment or*

*Administrative Adjustment Request (AAR).*

A change to the partnership's Federal return may affect its state return. This includes changes made as a result of an examination of the partnership return by the IRS. For more information, contact the state tax agency for the state in which the partnership return is filed.

## Other Forms, Returns, and Statements That May Be Required

- **Forms W-2 and W-3**, Wage and Tax Statement; and Transmittal of Wage and Tax Statements. Use these forms to report wages, tips, other compensation, and withheld income, social security and Medicare taxes for employees.
- **Form 720**, Quarterly Federal Excise Tax Return. Use Form 720 to report environmental excise taxes, communications and air transportation taxes, fuel taxes, luxury tax on passenger vehicles, manufacturers' taxes, ship passenger tax, and certain other excise taxes.
- **Form 940 or Form 940-EZ**, Employer's Annual Federal Unemployment (FUTA) Tax Return. The partnership may be liable for FUTA tax and may have to file Form 940 or Form 940-EZ if it paid wages of \$1,500 or more in any calendar quarter during the calendar year (or the preceding calendar year) or one or more employees worked for the partnership for some part of a day in any 20 different weeks during the calendar year (or the preceding calendar year).
- **Form 941**, Employer's Quarterly Federal Tax Return. Employers must file this form quarterly to report income tax withheld on wages and employer and employee social security and Medicare taxes. Agricultural employers must file **Form 943**, Employer's Annual Tax Return for Agricultural Employees, instead of Form 941, to report income tax withheld and employer and employee social security and Medicare taxes on farmworkers.
- **Form 945**, Annual Return of Withheld Federal Income Tax. Use this form to report income tax withheld from nonpayroll payments, including pensions, annuities, individual retirement accounts (IRAs), gambling winnings, and backup withholding.



See **Trust Fund Recovery Penalty** on page 5.

- **Forms 1042 and 1042-S**, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons; and Foreign Person's U.S. Source Income Subject to Withholding. Use these forms to report and send withheld tax on payments or distributions made to nonresident alien individuals, foreign partnerships, or foreign corporations to the extent these payments or distributions constitute gross income from sources within the United States that is not effectively connected



with a U.S. trade or business. A domestic partnership must also withhold tax on a foreign partner's distributive share of such income, including amounts that are not actually distributed. Withholding on amounts not previously distributed to a foreign partner must be made and paid over by the earlier of (a) the date on which Schedule K-1 is sent to that partner or (b) the 15th day of the 3rd month after the end of the partnership's tax year. For more information, see sections 1441 and 1442 and **Pub. 515**, Withholding of Tax on Nonresident Aliens and Foreign Corporations.

- **Form 1042-T**, Annual Summary and Transmittal of Forms 1042-S. Use Form 1042-T to transmit paper Forms 1042-S to the IRS.
- **Form 1096**, Annual Summary and Transmittal of U.S. Information Returns.
- **Form 1098**, Mortgage Interest Statement. Use this form to report the receipt from any individual of \$600 or more of mortgage interest (including points) in the course of the partnership's trade or business.
- **Forms 1099-A, B, INT, LTC, MISC, MSA, OID, R, and S**. You may have to file these information returns to report acquisitions or abandonments of secured property; proceeds from broker and barter exchange transactions; interest payments; payments of long-term care and accelerated death benefits; miscellaneous income payments; distributions from an Archer MSA; original issue discount; distributions from pensions, annuities, retirement or profit-sharing plans, IRAs, insurance contracts, etc.; and proceeds from real estate transactions. Also, use certain of these returns to report amounts that were received as a nominee on behalf of another person.

For more information, see the Instructions for Forms 1099, 1098, 5498, and W-2G.

**Important:** *Every partnership must file Forms 1099-MISC if, in the course of its trade or business, it makes payments of rents, commissions, or other fixed or determinable income (see section 6041) totaling \$600 or more to any one person during the calendar year.*

- **Form 5471**, Information Return of U.S. Persons With Respect to Certain Foreign Corporations. A partnership may have to file Form 5471 if it (a) controls a foreign corporation; or (b) acquires, disposes of, or owns 5% or more in value of the outstanding stock of a foreign corporation; or (c) owns stock in a corporation that is a controlled foreign corporation for an uninterrupted period of 30 days or more during any tax year of the foreign corporation, and it owned that stock on the last day of that year.
- **Form 5713**, International Boycott Report, is used by persons having operations in, or related to, a "boycotting" country, company, or national of a country, to report those operations and figure the loss of certain tax benefits. The partnership must give each partner a

copy of the Form 5713 filed by the partnership if there has been participation in, or cooperation with, an international boycott.

- **Form 8264**, Application for Registration of a Tax Shelter. Tax shelter organizers must file Form 8264 to get a tax shelter registration number from the IRS.
- **Form 8271**, Investor Reporting of Tax Shelter Registration Number. Partnerships that have acquired an interest in a tax shelter that is required to be registered use Form 8271 to report the tax shelter's registration number. Attach Form 8271 to any return on which a deduction, credit, loss, or other tax benefit attributable to a tax shelter is taken or any income attributable to a tax shelter is reported.
- **Form 8275**, Disclosure Statement. File Form 8275 to disclose items or positions, except those contrary to a regulation, that are not otherwise adequately disclosed on a tax return. The disclosure is made to avoid the parts of the accuracy-related penalty imposed for disregard of rules or substantial understatement of tax. Form 8275 is also used for disclosures relating to preparer penalties for understatements due to unrealistic positions or disregard of rules.
- **Form 8275-R**, Regulation Disclosure Statement, is used to disclose any item on a tax return for which a position has been taken that is contrary to Treasury regulations.
- **Forms 8288 and 8288-A**, U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests; and Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests. Use these forms to report and send withheld tax on the sale of U.S. real property by a foreign person. See section 1445 and the related regulations for additional information.
- **Form 8300**, Report of Cash Payments Over \$10,000 Received in a Trade or Business. File this form to report the receipt of more than \$10,000 in cash or foreign currency in one transaction or a series of related transactions.
- **Form 8308**, Report of a Sale or Exchange of Certain Partnership Interests, is used by a partnership to report the sale or exchange by a partner of all or part of a partnership interest where any money or other property received in exchange for the interest is attributable to unrealized receivables or inventory items.
- **Form 8594**, Asset Acquisition Statement Under Section 1060. Both the seller and buyer of a group of assets that makes up a trade or business must use this form to report such a sale if goodwill or going concern value attaches, or could attach, to such assets.
- **Form 8697**, Interest Computation Under the Look-Back Method for Completed Long-Term Contracts. Partnerships that are not closely held use this form to figure the interest due or to be refunded under the look-back method of section 460(b)(2) on certain long-term

contracts that are accounted for under either the percentage of completion-capitalized cost method or the percentage of completion method. Closely held partnerships should see the instructions on page 30 for line 25, item 10, of Schedule K-1 for details on the Form 8697 information they must provide to their partners.

- **Forms 8804, 8805, and 8813**, Annual Return for Partnership Withholding Tax (Section 1446); Foreign Partner's Information Statement of Section 1446 Withholding Tax; and Partnership Withholding Tax Payment (Section 1446). File Forms 8804 and 8805 if the partnership had effectively connected gross income and foreign partners for the tax year. Use Form 8813 to send installment payments of withheld tax based on effectively connected taxable income allocable to foreign partners.

**Exception:** *Publicly traded partnerships that do not elect to pay tax based on effectively connected taxable income do not file these forms. They must instead withhold tax on distributions to foreign partners and report and send payments using Forms 1042 and 1042-S. See Rev. Proc. 89-31, 1989-1 C.B. 895 and Rev. Proc. 92-66, 1992-2 C.B. 428 for more information.*

- **Form 8832**, Entity Classification Election. Except for a business entity automatically classified as a corporation, a business entity with at least two members may choose to be classified either as a partnership or an association taxable as a corporation. A domestic eligible entity with at least two members that does not file Form 8832 is classified under the default rules as a partnership. However, a foreign eligible entity with at least two members is classified under the default rules as a partnership only if at least one member does not have limited liability. File Form 8832 **only** if the entity does not want to be classified under these default rules or if it wants to change its classification.
- **Form 8865**, Return of U.S. Person With Respect To Certain Foreign Partnerships. A domestic partnership may have to file Form 8865 if it:

1. Controlled a foreign partnership (for example, it owned more than a 50% direct or indirect interest in the partnership).
2. Owned at least a 10% direct or indirect interest in a foreign partnership while U.S. persons controlled that partnership.
3. Had an acquisition, disposition, or change in proportional interest of a foreign partnership that:
  - a. Increased its direct interest to at least 10% or reduced its direct interest of at least 10% to less than 10%.
  - b. Changed its direct interest by at least a 10% interest.
4. Contributed property to a foreign partnership in exchange for a partnership interest if:

a. Immediately after the contribution, the partnership owned, directly or indirectly, at least a 10% interest in the foreign partnership; or

b. The fair market value of the property the partnership contributed to the foreign partnership in exchange for a partnership interest, when added to other contributions of property made to the foreign partnership during the preceding 12-month period, exceeds \$100,000.

Also, the domestic partnership may have to file Form 8865 to report certain dispositions by a foreign partnership of property it previously contributed to that foreign partnership if it was a partner at the time of the disposition.

For more details, including penalties for failing to file Form 8865, see Form 8865 and its separate instructions.

• **Form 8866, Interest Computation Under the Look-Back Method for Property Depreciated Under the Income Forecast Method.** Partnerships that are not closely held use this form to figure the interest due or to be refunded under the look-back method of section 167(g)(2) for certain property placed in service after September 13, 1995, depreciated under the income forecast method. Closely held partnerships should see the instructions on page 30 for line 25, item 19, of Schedule K-1 for details on the Form 8866 information they must provide to their partners.

• **Form 8876, Excise Tax on Structured Settlement Factoring Transactions.** Use Form 8876 to report and pay the 40% excise tax imposed under section 5891.

• **Statement of section 743(b) basis adjustments.** If the partnership is required to adjust the bases of partnership properties under section 743(b) because of a section 754 election on the sale or exchange of a partnership interest or on the death of a partner, the partnership must attach a statement to its return for the year of the transfer. The statement must list:

1. The name and identifying number of the transferee partner,
2. The computation of the adjustment, and
3. The partnership properties to which the adjustment has been allocated.

• **Tax Shelter Disclosure Statement.** For each reportable tax shelter transaction entered into **prior to January 1, 2003**, in which the partnership participated, directly or indirectly, it must attach a disclosure statement to its return for each year ending with or within the tax year of any partner whose Federal income tax liability is affected or reasonably expected to be affected by the partnership's participation in the transaction. In addition, for the first tax year a disclosure statement is attached to its return, the partnership must send a copy of the statement to the Internal Revenue Service, LM:PFTG:OTSA, Large & Mid-Size Business Division, 1111 Constitution Ave., N.W., Washington, DC 20224. If a transaction becomes a reportable transaction after the

partnership files its return, it must attach the statement to the following year's return (whether or not any partner's tax liability is affected for that year). The partnership is considered to have indirectly participated if it participated as a partner in a partnership or if it knows or has reason to know that the tax benefits claimed were derived from a reportable transaction.

Disclosure is required for a reportable transaction that is a listed transaction. A transaction is a listed transaction if it is the same as or substantially similar to a transaction that the IRS has determined to be a tax avoidance transaction and has identified as a listed transaction by notice, regulation, or other published guidance. See Notice 2001-51, 2001-34 I.R.B. 190, for transactions identified by the IRS as listed transactions. The listed transactions identified in this notice will be updated in future published guidance.

See Temporary Regulations section 1.6011-4T for more details, including:

1. Definitions of reportable transaction, listed transaction, and substantially similar.
2. Form and content of the disclosure statement.
3. Filing requirements for the disclosure statement.

For reportable transactions entered into **after December 31, 2002**, use **Form 8886, Reportable Transaction Disclosure Statement**, to disclose information for each reportable transaction in which the partnership participated, directly or indirectly. Form 8886 must be filed for each tax year ending with or within the tax year of any partner whose Federal income tax liability is affected or reasonably expected to be affected by the partnership's participation in the transaction. The following are reportable transactions.

- Any transaction the same as or substantially similar to tax avoidance transactions identified by the IRS.
- Any transaction offered under conditions of confidentiality.
- Any transaction for which the partnership has contractual protection against disallowance of the tax benefits.
- Any transaction resulting in a loss of at least \$5 million in any single year or \$10 million in any combination of years.
- Any transaction resulting in a book-tax difference of more than \$10 million on a gross basis.
- Any transaction resulting in a tax credit of more than \$250,000, if the partnership held the asset generating the credit for less than 45 days.

See the Instructions for Form 8886 for more details.

## Assembling the Return

When submitting Form 1065, organize the pages of the return in the following order:

- Pages 1–4,
- Schedule F (if required),
- Form 8825 (if required),
- Any other schedules in alphabetical order, and

- Any other forms in numerical order.

To assist us in processing the return, complete every applicable entry space on Form 1065 and Schedule K-1. **If you attach statements, do not write "See attached" instead of completing the entry spaces on the forms. Penalties may be assessed if the partnership files an incomplete return.**

If you need more space on the forms or schedules, attach separate sheets and place them at the end of the return. Use the same size and format as on the printed forms. **But show your totals on the printed forms.** Be sure to put the partnership's name and EIN on each sheet.

## Separately Stated Items

Partners must take into account separately (under section 702(a)) their distributive shares of the following items (whether or not they are actually distributed):

1. Ordinary income or loss from trade or business activities.
2. Net income or loss from rental real estate activities.
3. Net income or loss from other rental activities.
4. Gains and losses from sales or exchanges of capital assets.
5. Gains and losses from sales or exchanges of property described in section 1231.
6. Charitable contributions.
7. Dividends (passed through to corporate partners) that qualify for the dividends-received deduction.
8. Taxes described in section 901 paid or accrued to foreign countries and to possessions of the United States.
9. Other items of income, gain, loss, deduction, or credit, to the extent provided by regulations. Examples of such items include nonbusiness expenses, intangible drilling and development costs, amortizable basis of reforestation expenses, and soil and water conservation expenditures.

## Elections Made by the Partnership

Generally, the partnership decides how to figure taxable income from its operations. For example, it chooses the accounting method and depreciation methods it will use. The partnership also makes elections under the following sections:

1. Section 179 (election to expense certain tangible property).
2. Section 614 (definition of property— mines, wells, and other natural deposits). This election must be made before the partners figure their individual depletion allowances under section 613A(c)(7)(D).
3. Section 1033 (involuntary conversions).
4. Section 754 (manner of electing optional adjustment to basis of partnership property).



Under section 754, a partnership may elect to adjust the basis of partnership property when property is distributed or when a partnership interest is transferred. If the election is made with respect to a transfer of a partnership interest (section 743(b)) and the assets of the partnership constitute a trade or business for purposes of section 1060(c), then the value of any goodwill transferred must be determined in the manner provided in Regulations section 1.1060-1. Once an election is made under section 754, it applies both to all distributions and to all transfers made during the tax year and in all subsequent tax years unless the election is revoked. See Regulations section 1.754-1(c).

This election must be made in a statement that is filed with the partnership's timely filed return (including any extension) for the tax year during which the distribution or transfer occurs. The statement must include:

- The name and address of the partnership.
- A declaration that the partnership elects under section 754 to apply the provisions of section 734(b) and section 743(b).
- The signature of the general partner authorized to sign the partnership return.

The partnership can get an automatic 12-month extension to make the section 754 election provided corrective action is taken within 12 months of the original deadline for making the election. For details, see Regulations section 301.9100-2.

See section 754 and the related regulations for more information.

If there is a distribution of property consisting of an interest in another partnership, see section 734(b).

The partnership is required to attach a statement for any section 743(b) basis adjustments. See page 8 for details.

## Elections Made by Each Partner

Elections under the following sections are made by each partner separately on the partner's tax return:

1. Section 59(e) (election to deduct ratably certain qualified expenditures such as intangible drilling costs, mining exploration expenses, or research and experimental expenditures).
2. Section 108 (income from discharge of indebtedness).
3. Section 617 (deduction and recapture of certain mining exploration expenditures paid or incurred).
4. Section 901 (foreign tax credit).

## Partner's Dealings With Partnership

If a partner engages in a transaction with his or her partnership, other than in his or her capacity as a partner, the partner is treated as not being a member of the partnership for that transaction. Special

rules apply to sales or exchanges of property between partnerships and certain persons, as explained in **Pub. 541, Partnerships**.

## Contributions to the Partnership

Generally, no gain (loss) is recognized to the partnership or any of the partners when property is contributed to the partnership in exchange for an interest in the partnership. This rule does not apply to any gain realized on a transfer of property to a partnership that would be treated as an investment company (within the meaning of section 351) if the partnership were incorporated. If, as a result of a transfer of property to a partnership, there is a direct or indirect transfer of money or other property to the transferring partner, the partner may have to recognize gain on the exchange.

The basis to the partnership of property contributed by a partner is the adjusted basis in the hands of the partner at the time it was contributed, plus any gain recognized (under section 721(b)) by the partner at that time. See section 723 for more information.

## Dispositions of Contributed Property

If the partnership disposes of property contributed to the partnership by a partner, income, gain, loss, and deductions from that property must be allocated among the partners to take into account the difference between the property's basis and its FMV at the time of the contribution.

For property contributed to the partnership, the contributing partner must recognize gain or loss on a distribution of the property to another partner within 5 years of being contributed. For property contributed after June 8, 1997, the 5-year period is generally extended to 7 years. The gain or loss is equal to the amount that the contributing partner should have recognized if the property had been sold for its FMV when distributed, because of the difference between the property's basis and its FMV at the time of contribution.

See section 704(c) for details and other rules on dispositions of contributed property. See section 724 for the character of any gain or loss recognized on the disposition of unrealized receivables, inventory items, or capital loss property contributed to the partnership by a partner.

## Recognition of Precontribution Gain on Certain Partnership Distributions

A partner who contributes appreciated property to the partnership must include in income any precontribution gain to the extent the FMV of other property (other

than money) distributed to the partner by the partnership exceeds the adjusted basis of his or her partnership interest just before the distribution. Precontribution gain is the net gain, if any, that would have been recognized under section 704(c)(1)(B) if the partnership had distributed to another partner all the property that had been contributed to the partnership by the distributee partner within 5 years of the distribution and that was held by the partnership just before the distribution. For property contributed after June 8, 1997, the 5-year period is generally extended to 7 years.

Appropriate basis adjustments are to be made to the adjusted basis of the distributee partner's interest in the partnership and the partnership's basis in the contributed property to reflect the gain recognized by the partner.

For more details and exceptions, see **Pub. 541**.

## Unrealized Receivables and Inventory Items

Generally, if a partner sells or exchanges a partnership interest where unrealized receivables or inventory items are involved, the transferor partner must notify the partnership, in writing, within 30 days of the exchange. The partnership must then file **Form 8308**, Report of a Sale or Exchange of Certain Partnership Interests.

If a partnership distributes unrealized receivables or substantially appreciated inventory items in exchange for all or part of a partner's interest in other partnership property (including money), treat the transaction as a sale or exchange between the partner and the partnership. Treat the partnership gain (loss) as ordinary income (loss). The income (loss) is specially allocated only to partners other than the distributee partner.

If a partnership gives other property (including money) for all or part of that partner's interest in the partnership's unrealized receivables or substantially appreciated inventory items, treat the transaction as a sale or exchange of the property.

See **Rev. Rul. 84-102, 1984-2 C.B. 119**, for information on the tax consequences that result when a new partner joins a partnership that has liabilities and unrealized receivables. Also, see **Pub. 541** for more information on unrealized receivables and inventory items.

## Passive Activity Limitations

In general, section 469 limits the amount of losses, deductions, and credits that partners may claim from "passive activities." The passive activity limitations do not apply to the partnership. Instead, they apply to each partner's share of any income or loss and credit attributable to a passive activity. Because the treatment of each partner's share of partnership

income or loss and credit depends on the nature of the activity that generated it, the partnership must report income or loss and credits separately for each activity.

The following instructions and the instructions for Schedules K and K-1 (pages 21–31) explain the applicable passive activity limitation rules and specify the type of information the partnership must provide to its partners for each activity. If the partnership has more than one activity, it must report information for each activity on an attachment to Schedules K and K-1.

Generally, passive activities include **(a)** activities that involve the conduct of a trade or business if the partner does not materially participate in the activity; and **(b)** all rental activities (defined below), regardless of the partner's participation. For exceptions, see **Activities That Are Not Passive Activities** below. The level of each partner's participation in an activity must be determined by the partner.

The passive activity rules provide that losses and credits from passive activities can generally be applied only against income and tax from passive activities. Thus, passive losses and credits cannot be applied against income from salaries, wages, professional fees, or a business in which the taxpayer materially participates; against "portfolio income" (defined on page 11); or against the tax related to any of these types of income.

Special provisions apply to certain activities. First, the passive activity limitations must be applied separately with respect to a net loss from passive activities held through a publicly traded partnership. Second, special rules require that net income from certain activities that would otherwise be treated as passive income must be recharacterized as nonpassive income for purposes of the passive activity limitations.

To allow each partner to correctly apply the passive activity limitations, the partnership must report income or loss and credits separately for each of the following types of activities and income: trade or business activities, rental real estate activities, rental activities other than rental real estate, and portfolio income.

## Activities That Are Not Passive Activities

Passive activities **do not** include:

1. Trade or business activities in which the partner materially participated for the tax year.
2. Any rental real estate activity in which the partner materially participated if the partner met both of the following conditions for the tax year:
  - a. More than half of the personal services the partner performed in trades or businesses were performed in real property trades or businesses in which he or she materially participated **and**
  - b. The partner performed more than 750 hours of services in real property

trades or businesses in which he or she materially participated.

**Note:** For a partner that is a closely held C corporation (defined in section 465(a)(1)(B)), the above conditions are treated as met if more than 50% of the corporation's gross receipts are from real property trades or businesses in which the corporation materially participated.

For purposes of this rule, each interest in rental real estate is a separate activity, unless the partner elects to treat all interests in rental real estate as one activity.

If the partner is married filing jointly, either the partner or his or her spouse must separately meet both of the above conditions, without taking into account services performed by the other spouse.

A real property trade or business is any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business. Services the partner performed as an employee are not treated as performed in a real property trade or business unless he or she owned more than 5% of the stock (or more than 5% of the capital or profits interest) in the employer.

**3.** An interest in an oil or gas well drilled or operated under a working interest if at any time during the tax year the partner held the working interest directly or through an entity that did not limit the partner's liability (for example, an interest as a general partner). This exception applies regardless of whether the partner materially participated for the tax year.

**4.** The rental of a dwelling unit used by a partner for personal purposes during the year for more than the **greater of 14 days or 10%** of the number of days that the residence was rented at fair rental value.

**5.** An activity of trading personal property for the account of owners of interests in the activity. For purposes of this rule, personal property means property that is actively traded, such as stocks, bonds, and other securities. See Temporary Regulations section 1.469-1T(e)(6).

## Trade or Business Activities

A trade or business activity is an activity (other than a rental activity or an activity treated as incidental to an activity of holding property for investment) that:

1. Involves the conduct of a trade or business (within the meaning of section 162),
2. Is conducted in anticipation of starting a trade or business, or
3. Involves research or experimental expenditures deductible under section 174 (or that would be if you chose to deduct rather than capitalize them).

If the partner does not materially participate in the activity, a trade or business activity held through a

partnership is generally a passive activity of the partner.

Each partner must determine if he or she materially participated in an activity. As a result, while the partnership's overall trade or business income (loss) is reported on page 1 of Form 1065, the specific income and deductions from each separate trade or business activity must be reported on attachments to Form 1065. Similarly, while each partner's allocable share of the partnership's overall trade or business income (loss) is reported on line 1 of Schedule K-1, each partner's allocable share of the income and deductions from each trade or business activity must be reported on attachments to each Schedule K-1. See **Passive Activity Reporting Requirements** on page 13 for more information.

## Rental Activities

Generally, except as noted below, if the gross income from an activity consists of amounts paid principally for the use of real or personal tangible property held by the partnership, the activity is a rental activity.

There are several exceptions to this general rule. Under these exceptions, an activity involving the use of real or personal tangible property is not a rental activity if any of the following apply:

- The **average period of customer use** (defined below) for such property is 7 days or less.
- The average period of customer use for such property is 30 days or less and **significant personal services** (defined on page 11) are provided by or on behalf of the partnership.
- **Extraordinary personal services** (defined on page 11) are provided by or on behalf of the partnership.
- The rental of such property is treated as **incidental** to a nonrental activity of the partnership under Temporary Regulations section 1.469-1T(e)(3)(vi) and Regulations section 1.469-1(e)(3)(vi).
- The partnership customarily makes the property available during defined business hours for nonexclusive use by various customers.
- The partnership provides property for use in a nonrental activity of a partnership or joint venture in its capacity as an owner of an interest in such partnership or joint venture. Whether the partnership provides property used in an activity of another partnership or of a joint venture in the partnership's capacity as an owner of an interest in the partnership or joint venture is determined on the basis of all the facts and circumstances.

In addition, a guaranteed payment described in section 707(c) is not income from a rental activity under any circumstances.

### Average period of customer use.

Figure the average period of customer use for a class of property by dividing the total number of days in all rental periods by the number of rentals during the tax year. If the activity involves renting more



than one class of property, multiply the average period of customer use of each class by the ratio of the gross rental income from that class to the activity's total gross rental income. The activity's average period of customer use equals the sum of these class-by-class average periods weighted by gross income. See Regulations section 1.469-1(e)(3)(iii).

**Significant personal services.** Personal services include only services performed by individuals. To determine if personal services are significant personal services, consider all the relevant facts and circumstances. Relevant facts and circumstances include how often the services are provided, the type and amount of labor required to perform the services, and the value of the services in relation to the amount charged for use of the property.

The following services are not considered in determining whether personal services are significant:

- Services necessary to permit the lawful use of the rental property.
- Services performed in connection with improvements or repairs to the rental property that extend the useful life of the property substantially beyond the average rental period.
- Services provided in connection with the use of any improved real property that are similar to those commonly provided in connection with long-term rentals of high-grade commercial or residential property. Examples include cleaning and maintenance of common areas, routine repairs, trash collection, elevator service, and security at entrances.

**Extraordinary personal services.** Services provided in connection with making rental property available for customer use are extraordinary personal services only if the services are performed by individuals and the customers' use of the rental property is incidental to their receipt of the services.

For example, a patient's use of a hospital room generally is incidental to the care received from the hospital's medical staff. Similarly, a student's use of a dormitory room in a boarding school is incidental to the personal services provided by the school's teaching staff.

**Rental activity incidental to a nonrental activity.** An activity is not a rental activity if the rental of the property is incidental to a nonrental activity, such as the activity of holding property for investment, a trade or business activity, or the activity of dealing in property.

Rental of property is **incidental** to an **activity of holding property for investment** if both of the following apply:

- The main purpose for holding the property is to realize a gain from the appreciation of the property.
- The gross rental income from such property for the tax year is less than 2% of the smaller of the property's **unadjusted basis** or its FMV.

Rental of property is **incidental** to a **trade or business activity** if all of the following apply:

- The partnership owns an interest in the trade or business at all times during the year.
- The rental property was mainly used in the trade or business activity during the tax year or during at least 2 of the 5 preceding tax years.
- The gross rental income from the property for the tax year is less than 2% of the smaller of the property's **unadjusted basis** or its FMV.

The sale or exchange of property that is both rented and sold or exchanged during the tax year (where the gain or loss is recognized) is treated as incidental to the activity of dealing in property if, at the time of the sale or exchange, the property was held primarily for sale to customers in the ordinary course of the partnership's trade or business.

See Temporary Regulations section 1.469-1T(e)(3) and Regulations section 1.469-1(e)(3) for more information on the definition of rental activities for purposes of the passive activity limitations.

**Reporting of rental activities.** In reporting the partnership's income or losses and credits from rental activities, the partnership must separately report rental real estate activities and rental activities other than rental real estate activities.

Partners who actively participate in a rental real estate activity may be able to deduct part or all of their rental real estate losses (and the deduction equivalent of rental real estate credits) against income (or tax) from nonpassive activities. The combined amount of rental real estate losses and the deduction equivalent of rental real estate credits from all sources (including rental real estate activities not held through the partnership) that may be claimed is limited to \$25,000. This \$25,000 amount is generally reduced for high-income partners.

Report rental real estate activity income (loss) on **Form 8825**, Rental Real Estate Income and Expenses of a Partnership or an S Corporation, and line 2 of Schedules K and K-1 rather than on page 1 of Form 1065. Report credits related to rental real estate activities on lines 12b and 12c and low-income housing credits on line 12a of Schedules K and K-1.

Report income (loss) from rental activities other than rental real estate on line 3 and credits related to rental activities other than rental real estate on line 12d of Schedules K and K-1.

### Portfolio Income

Generally, portfolio income includes all gross income, other than income derived in the ordinary course of a trade or business, that is attributable to interest; dividends; royalties; income from a real estate investment trust, a regulated investment company, a real estate mortgage investment conduit, a common trust fund, a controlled foreign

corporation, a qualified electing fund, or a cooperative; income from the disposition of property that produces income of a type defined as portfolio income; and income from the disposition of property held for investment. See **Self-Charged Interest** below for an exception.

Solely for purposes of the preceding paragraph, gross income derived in the ordinary course of a trade or business includes (and portfolio income, therefore, does not include) only the following types of income:

- Interest income on loans and investments made in the ordinary course of a trade or business of lending money.
- Interest on accounts receivable arising from the performance of services or the sale of property in the ordinary course of a trade or business of performing such services or selling such property, but only if credit is customarily offered to customers of the business.
- Income from investments made in the ordinary course of a trade or business of furnishing insurance or annuity contracts or reinsuring risks underwritten by insurance companies.
- Income or gain derived in the ordinary course of an activity of trading or dealing in any property if such activity constitutes a trade or business (unless the dealer held the property for investment at any time before such income or gain is recognized).
- Royalties derived by the taxpayer in the ordinary course of a trade or business of licensing intangible property.
- Amounts included in the gross income of a patron of a cooperative by reason of any payment or allocation to the patron based on patronage occurring with respect to a trade or business of the patron.
- Other income identified by the IRS as income derived by the taxpayer in the ordinary course of a trade or business.

See Temporary Regulations section 1.469-2T(c)(3) for more information on portfolio income.

Report portfolio income on line 4 of Schedules K and K-1, rather than on page 1 of Form 1065. Report deductions related to portfolio income on line 10 of Schedules K and K-1.

### Self-Charged Interest

Certain "self-charged" interest income and expense may be treated as passive activity gross income and passive activity deductions if the loan proceeds are used in a passive activity. Generally, self-charged interest income and expense result from loans to and from the partnership and its partners. It also includes loans between the partnership and another partnership if each owner in the borrowing entity has the same proportional ownership interest in the lending entity. See Regulations section 1.469-7 for details.

### Grouping Activities

Generally, one or more trade or business activities or rental activities may be treated as a single activity if the activities



make up an appropriate economic unit for the measurement of gain or loss under the passive activity rules. Whether activities make up an appropriate economic unit depends on all the relevant facts and circumstances. The factors given the greatest weight in determining whether activities make up an appropriate economic unit are:

- Similarities and differences in types of trades or businesses.
- The extent of common control.
- The extent of common ownership.
- Geographical location.
- Reliance between or among the activities.

**Example.** The partnership has a significant ownership interest in a bakery and a movie theater in Baltimore and a bakery and a movie theater in Philadelphia. Depending on the relevant facts and circumstances, there may be more than one reasonable method for grouping the partnership's activities. For instance, the following groupings may or may not be permissible:

- A single activity,
- A movie theater activity and a bakery activity,
- A Baltimore activity and a Philadelphia activity, or
- Four separate activities.

Once the partnership chooses a grouping under these rules, it must continue using that grouping in later tax years unless a material change in the facts and circumstances makes it clearly inappropriate.

The IRS may regroup the partnership's activities if the partnership's grouping fails to reflect one or more appropriate economic units and one of the primary purposes of the grouping is to avoid the passive activity limitations.

**Limitation on grouping certain activities.** The following activities may not be grouped together:

1. A rental activity with a trade or business activity unless the activities being grouped together make up an appropriate economic unit and
  - a. The rental activity is insubstantial relative to the trade or business activity or vice versa or
  - b. Each owner of the trade or business activity has the same proportionate ownership interest in the rental activity. If so, the portion of the rental activity involving the rental of property to be used in the trade or business activity may be grouped with the trade or business activity.
2. An activity involving the rental of real property with an activity involving the rental of personal property (except personal property provided in connection with the real property or vice versa).
3. Any activity with another activity in a different type of business and in which the partnership holds an interest as a limited partner or as a limited entrepreneur (as defined in section 464(e)(2)) if that other activity engages in holding, producing, or distributing motion

picture films or videotapes; farming; leasing section 1245 property; or exploring for or exploiting oil and gas resources or geothermal deposits.

**Activities conducted through other partnerships.** Once a partnership determines its activities under these rules, the partnership as a partner may use these rules to group those activities with:

- Each other,
- Activities conducted directly by the partnership, or
- Activities conducted through other partnerships.

A partner may not treat as separate activities those activities grouped together by a partnership.

## Recharacterization of Passive Income

Under Temporary Regulations section 1.469-2T(f) and Regulations section 1.469-2(f), net passive income from certain passive activities must be treated as nonpassive income. Net passive income is the excess of an activity's passive activity gross income over its passive activity deductions (current year deductions and prior year unallowed losses).

Income from the following six sources is subject to recharacterization. Note that any net passive income recharacterized as nonpassive income is treated as investment income for purposes of figuring investment interest expense limitations if it is from (a) an activity of renting substantially nondepreciable property from an equity-financed lending activity or (b) an activity related to an interest in a pass-through entity that licenses intangible property.

**1. Significant participation passive activities.** A significant participation passive activity is any trade or business activity in which the partner both participates for more than 100 hours during the tax year and does not materially participate. Because each partner must determine the partner's level of participation, the partnership will not be able to identify significant participation passive activities.

**2. Certain nondepreciable rental property activities.** Net passive income from a rental activity is nonpassive income if less than 30% of the unadjusted basis of the property used or held for use by customers in the activity is subject to depreciation under section 167.

**3. Passive equity-financed lending activities.** If the partnership has net income from a passive equity-financed lending activity, the smaller of the net passive income or the equity-financed interest income from the activity is nonpassive income.

**Note:** *The amount of income from the activities in paragraphs 1 through 3 that any partner will be required to recharacterize as nonpassive income may be limited under Temporary Regulations section 1.469-2T(f)(8). Because the partnership will not have*

*information regarding all of a partner's activities, it must identify all partnership activities meeting the definitions in paragraphs 2 and 3 as activities that may be subject to recharacterization.*

**4. Rental of property incidental to a development activity.** Net rental activity income is the excess of passive activity gross income from renting or disposing of property over passive activity deductions (current year deductions and prior year unallowed losses) that are reasonably allocable to the rented property. Net rental activity income is nonpassive income for a partner if all of the following apply:

- The partnership recognizes gain from the sale, exchange, or other disposition of the rental property during the tax year.
- The use of the item of property in the rental activity started less than 12 months before the date of disposition. The use of an item of rental property begins on the first day that (a) the partnership owns an interest in the property; (b) substantially all of the property is either rented or held out for rent and ready to be rented; and (c) no significant value-enhancing services remain to be performed.
- The partner materially or significantly participated for any tax year in an activity that involved performing services to enhance the value of the property (or any other item of property, if the basis of the property disposed of is determined in whole or in part by reference to the basis of that item of property).

Because the partnership cannot determine a partner's level of participation, the partnership must identify net income from property described above (without regard to the partner's level of participation) as income that may be subject to recharacterization.

**5. Rental of property to a nonpassive activity.** If a taxpayer rents property to a trade or business activity in which the taxpayer materially participates, the taxpayer's net rental activity income from the property is nonpassive income.

**6. Acquisition of an interest in a pass-through entity that licenses intangible property.** Generally, net royalty income from intangible property is nonpassive income if the taxpayer acquired an interest in the pass-through entity after the pass-through entity created the intangible property or performed substantial services, or incurred substantial costs in developing or marketing the intangible property. "Net royalty income" means the excess of passive activity gross income from licensing or transferring any right in intangible property over passive activity deductions (current year deductions and prior year unallowed losses) that are reasonably allocable to the intangible property.

See Temporary Regulations section 1.469-2T(f)(7)(iii) for exceptions to this rule.

## Passive Activity Reporting Requirements

To allow partners to correctly apply the passive activity loss and credit rules, any partnership that carries on more than one activity must:

1. Provide an attachment for each activity conducted through the partnership that identifies the type of activity conducted (trade or business, rental real estate, rental activity other than rental real estate, or investment).

2. On the attachment for each activity, provide a schedule, using the same line numbers as shown on Schedule K-1, detailing the net income (loss), credits, and all items required to be separately stated under section 702(a) from each trade or business activity, from each rental real estate activity, from each rental activity other than a rental real estate activity, and from investments.

3. Identify the net income (loss) and credits from each oil or gas well drilled or operated under a working interest that any partner (other than a partner whose only interest in the partnership during the year is as a limited partner) holds through the partnership. Further, if any partner had an interest as a general partner in the partnership during less than the entire year, the partnership must identify both the disqualified deductions from each well that the partner must treat as passive activity deductions, and the ratable portion of the gross income from each well that the partner must treat as passive activity gross income.

4. Identify the net income (loss) and the partner's share of partnership interest expense from each activity of renting a dwelling unit that any partner uses for personal purposes during the year for more than the greater of 14 days or 10% of the number of days that the residence is rented at fair rental value.

5. Identify the net income (loss) and the partner's share of partnership interest expense from each activity of trading personal property conducted through the partnership.

6. For any gain (loss) from the disposition of an interest in an activity or of an interest in property used in an activity (including dispositions before 1987 from which gain is being recognized after 1986):

a. Identify the activity in which the property was used at the time of disposition.

b. If the property was used in more than one activity during the 12 months preceding the disposition, identify the activities in which the property was used and the adjusted basis allocated to each activity.

c. For gains only, if the property was substantially appreciated at the time of the disposition and the applicable holding period specified in Regulations section 1.469-2(c)(2)(iii)(A) was not satisfied, identify the amount of the nonpassive gain and indicate whether the gain is investment income under the provisions

of Regulations section 1.469-2(c)(2)(iii)(F).

7. Specify the amount of gross portfolio income, the interest expense properly allocable to portfolio income, and expenses other than interest expense that are clearly and directly allocable to portfolio income.

8. Identify separately any of the following types of payments to partners:

a. Payments to a partner for services other than in the partner's capacity as a partner under section 707(a).

b. Guaranteed payments to a partner for services under section 707(c).

c. Guaranteed payments for use of capital.

d. If section 736(a)(2) payments are made for unrealized receivables or for goodwill, the amount of the payments and the activities to which the payments are attributable.

e. If section 736(b) payments are made, the amount of the payments and the activities to which the payments are attributable.

9. Identify the ratable portion of any section 481 adjustment (whether a net positive or a net negative adjustment) allocable to each partnership activity.

10. Identify the amount of gross income from each oil or gas property of the partnership.

11. Identify any gross income from sources that are specifically excluded from passive activity gross income, including:

a. Income from intangible property if the partner is an individual and the partner's personal efforts significantly contributed to the creation of the property.

b. Income from state, local, or foreign income tax refunds.

c. Income from a covenant not to compete (in the case of a partner who is an individual and who contributed the covenant to the partnership).

12. Identify any deductions that are not passive activity deductions.

13. If the partnership makes a full or partial disposition of its interest in another entity, identify the gain (loss) allocable to each activity conducted through the entity, and the gain allocable to a passive activity that would have been recharacterized as nonpassive gain had the partnership disposed of its interest in property used in the activity (because the property was substantially appreciated at the time of the disposition, and the gain represented more than 10% of the partner's total gain from the disposition).

14. Identify the following items from activities that may be subject to the recharacterization rules under Temporary Regulations section 1.469-2T(f) and Regulations section 1.469-2(f):

a. Net income from an activity of renting substantially nondepreciable property.

b. The smaller of equity-financed interest income or net passive income from an equity-financed lending activity.

c. Net rental activity income from property that was developed (by the

partner or the partnership), rented, and sold within 12 months after the rental of the property commenced.

d. Net rental activity income from the rental of property by the partnership to a trade or business activity in which the partner had an interest (either directly or indirectly).

e. Net royalty income from intangible property if the partner acquired the partner's interest in the partnership after the partnership created the intangible property or performed substantial services, or incurred substantial costs in developing or marketing the intangible property.

15. Identify separately the credits from each activity conducted by or through the partnership.

16. Identify the partner's distributive share of the partnership's self-charged interest income or expense (see **Self-Charged Interest** on page 11.

a. **Loans between a partner and the partnership.** Identify the lending or borrowing partner's share of the self-charged interest income or expense.

If the partner made the loan to the partnership, also identify the activity in which the loan proceeds were used. If the loan proceeds were used in more than one activity, allocate the interest to each activity based on the amount of the proceeds used in each activity.

b. **Loans between the partnership and another partnership or an S corporation.** If the partnership's partners have the same proportional ownership interest in the partnership and the other partnership or S corporation, identify each partner's share of the interest income or expense from the loan. If the partnership was the borrower, also identify the activity in which the loan proceeds were used. If the loan proceeds were used in more than one activity, allocate the interest to each activity based on the amount of the proceeds used in each activity.

## Extraterritorial Income Exclusion

The partnership may exclude extraterritorial income to the extent of qualifying foreign trade income. For details and to figure the amount of the exclusion, see **Form 8873**, Extraterritorial Income Exclusion, and its separate instructions. The partnership must report the extraterritorial income exclusion on its return as follows:

1. If the partnership met the foreign economic process requirements explained in the Instructions for Form 8873, it may report the exclusion as a nonseparately stated item on whichever of the following lines apply to that activity:

- Form 1065, page 1, line 20;
- Form 8825, line 15; or
- Form 1065, Schedule K, line 3b.

In addition, the partnership must report as an item of information on Schedule K-1, line 25, the partner's distributive share of foreign trading gross receipts from Form 8873, line 15.



2. If the foreign trading gross receipts of the partnership for the tax year are \$5 million or less and the partnership did not meet the foreign economic process requirements, it may **not** report the extraterritorial income exclusion as a nonseparately stated item on its return.

Instead, the partnership must report the following separately stated items to the partners on Schedule K-1, line 25:

- The partner's distributive share of foreign trading gross receipts from the partnership's Form 8873, line 15.
- The partner's distributive share of the extraterritorial income exclusion from the partnership's Form 8873, line 55, and identify the activity to which the exclusion relates.

**Note:** Upon request of a partner, the partnership should furnish a copy of the partnership's Form 8873 if that partner has a reduction for international boycott operations, illegal bribes, kickbacks, etc.

## Specific Instructions

These instructions follow the line numbers on the first page of Form 1065. The accompanying schedules will be discussed separately. Specific instructions for most of the lines are provided. Lines that are not discussed are self-explanatory.

### Fill in all applicable lines and schedules.

Enter any items specially allocated to the partners on the appropriate line of the applicable partner's Schedule K-1. Enter the total amount on the appropriate line of Schedule K. **Do not** enter separately stated amounts on the numbered lines on Form 1065, page 1, or on Schedule A or Schedule D.

File all four pages of Form 1065. However, if the answer to Question 5 of Schedule B is **Yes**, Schedules L, M-1, and M-2 on page 4 are optional. Also attach a Schedule K-1 to Form 1065 for each partner.

File only one Form 1065 for each partnership. Mark "Duplicate Copy" on any copy you give to a partner.

If a syndicate, pool, joint venture, or similar group files Form 1065, it must attach a copy of the agreement and all amendments to the return, unless a copy has previously been filed.

**Note:** A foreign partnership required to file a return generally must report all of its foreign and U.S. source income. For rules regarding whether a foreign partnership must file Form 1065, see **Who Must File** on page 2.

## General Information

### Name, Address, and Employer Identification Number

Use the label that was mailed to the partnership. Cross out any errors and print the correct information on the label.

**Name.** If the partnership did not receive a label, print or type the legal name of the partnership as it appears in the partnership agreement.

If the partnership has changed its name, check box G(3).

**Address.** Include the suite, room, or other unit number after the street address. If a preaddressed label is used, include this information on the label.

If the Post Office does not deliver mail to the street address and the partnership has a P.O. box, show the box number instead.

If the partnership's address is outside the United States or its possessions or territories, enter the information on the line for "City or town, state, and ZIP code" in the following order: city, province or state, and the foreign country. Follow the foreign country's practice in placing the postal code in the address. **Do not** abbreviate the country name.

If the partnership has had a change of address, check box G(4).

If the partnership changes its mailing address after filing its return, it can notify the IRS by filing **Form 8822**, Change of Address.

**Employer identification number (EIN).** Show the correct EIN in item D on page 1 of Form 1065. If the partnership does not have an EIN, it must apply for one on **Form SS-4**, Application for Employer Identification Number. Form SS-4 has information on how to apply for an EIN by mail or by telephone. If the partnership has not received its EIN by the time the return is due, write "Applied for" in the space for the EIN. See **Pub. 583**, Starting a Business and Keeping Records, for more information.

**Do not** request a new EIN for a partnership that terminated because of a sale or exchange of at least 50% of the total interests in partnership capital and profits.

### Items A and C

Enter the applicable activity name and the code number from the list beginning on page 33.

For example, if, as its principal business activity, the partnership **(a)** purchases raw materials, **(b)** subcontracts out for labor to make a finished product from the raw materials, and **(c)** retains title to the goods, the partnership is considered to be a manufacturer and must enter "Manufacturer" in item A and enter in item C one of the codes (311110 through 339900) listed under "Manufacturing" beginning on page 33.

## Item F—Total Assets

You are not required to complete item F if the answer to Question 5 of Schedule B is **Yes**.


If you are required to complete this item, enter the partnership's total assets at the end of the tax year, as determined by the accounting method regularly used in keeping the partnership's books and records. If there were no assets at the end of the tax year, enter "0."

## Item G

**Do not** check "Final return" (box G(2)) for a partnership that terminated because of a sale or exchange of at least 50% of the total interests in partnership capital and profits. However, be sure to file a return for the short year ending on the date of termination. See **Termination of the Partnership** on page 3.

For information on amended returns, see page 6.

## Income

 Report only trade or business activity income on lines 1a through 8. **Do not report rental activity income or portfolio income on these lines.** See the instructions on **Passive Activity Limitations** beginning on page 9 for definitions of rental income and portfolio income. Rental activity income and portfolio income are reported on Schedules K and K-1. Rental real estate activities are also reported on Form 8825.

Do not include any tax-exempt income on lines 1a through 8. A partnership that receives any tax-exempt income other than interest, or holds any property or engages in any activity that produces tax-exempt income reports the amount of this income on line 20 of Schedules K and K-1.

Report tax-exempt interest income, including exempt-interest dividends received as a shareholder in a mutual fund or other regulated investment company, on line 19 of Schedules K and K-1.

See **Deductions** on page 15 for information on how to report expenses related to tax-exempt income.

If the partnership has had debt discharged resulting from a title 11 bankruptcy proceeding or while insolvent, see **Form 982**, Reduction of Tax Attributes Due to Discharge of Indebtedness, and **Pub. 908**, Bankruptcy Tax Guide.

### Line 1a—Gross Receipts or Sales

Enter the gross receipts or sales from all trade or business operations except those that must be reported on lines 4 through 7. For example, do not include gross receipts from farming on this line. Instead, show the net profit (loss) from farming on line 5. Also, do not include on line 1a rental activity income or portfolio income.

In general, advance payments are reported in the year of receipt. To report



income from long-term contracts, see section 460. For special rules for reporting certain advance payments for goods and long-term contracts, see Regulations section 1.451-5. For permissible methods for reporting advance payments for services by an accrual method partnership, see Rev. Proc. 71-21, 1971-2 C.B. 549.

**Installment sales.** Generally, the installment method cannot be used for dealer dispositions of property. A "dealer disposition" is any disposition of:

1. Personal property by a person who regularly sells or otherwise disposes of personal property of the same type on the installment plan or
2. Real property held for sale to customers in the ordinary course of the taxpayer's trade or business.

**Exception.** These restrictions on using the installment method do not apply to dispositions of property used or produced in a farming business or sales of timeshares and residential lots. However, if the partnership elects to report dealer dispositions of timeshares and residential lots on the installment method, each partner's tax liability must be increased by the partner's allocable share of the interest payable under section 453(l)(3).

Enter on line 1a the gross profit on collections from installment sales for any of the following:

- Dealer dispositions of property before March 1, 1986.
- Dispositions of property used or produced in the trade or business of farming.
- Certain dispositions of timeshares and residential lots reported under the installment method.

Attach a schedule showing the following information for the current year and the 3 preceding years:

- Gross sales.
- Cost of goods sold.
- Gross profits.
- Percentage of gross profits to gross sales.
- Amount collected.
- Gross profit on amount collected.

## Line 2—Cost of Goods Sold

See the instructions for Schedule A on page 19.

## Line 4—Ordinary Income (Loss) From Other Partnerships, Estates, and Trusts

Enter the ordinary income (loss) shown on Schedule K-1 (Form 1065) or Schedule K-1 (Form 1041), or other ordinary income (loss) from a foreign partnership, estate, or trust. Show the partnership's, estate's, or trust's name, address, and EIN on a separate statement attached to this return. If the amount entered is from more than one source, identify the amount from each source.

**Do not** include portfolio income or rental activity income (loss) from other

partnerships, estates, or trusts on this line. Instead, report these amounts on the applicable lines of Schedules K and K-1, or on line 20a of Form 8825 if the amount is from a rental real estate activity.

Ordinary income or loss from another partnership that is a publicly traded partnership is not reported on this line. Instead, report the amount separately on line 7 of Schedules K and K-1.

Treat shares of other items separately reported on Schedule K-1 issued by the other entity as if the items were realized or incurred by this partnership.

If there is a loss from another partnership, the amount of the loss that may be claimed is subject to the at-risk and basis limitations as appropriate.

If the tax year of your partnership does not coincide with the tax year of the other partnership, estate, or trust, include the ordinary income (loss) from the other entity in the tax year in which the other entity's tax year ends.

## Line 5—Net Farm Profit (Loss)


Enter the partnership's net farm profit (loss) from **Schedule F (Form 1040)**, Profit or Loss From Farming. Attach Schedule F (Form 1040) to Form 1065. **Do not** include on this line any farm profit (loss) from other partnerships. Report those amounts on line 4. In figuring the partnership's net farm profit (loss), do not include any section 179 expense deduction; this amount must be separately stated.

Also report the partnership's fishing income on this line.

For a special rule concerning the method of accounting for a farming partnership with a corporate partner and for other tax information on farms, see **Pub. 225**, Farmer's Tax Guide.

**Note:** *Because the election to deduct the expenses of raising any plant with a preproductive period of more than 2 years is made by the partner and not the partnership, farm partnerships that are not required to use an accrual method should not capitalize such expenses. Instead, state them separately on an attachment to Schedule K, line 24, and on Schedule K-1, line 25, Supplemental Information. See Regulations section 1.263A-4 for more information.*

## Line 6—Net Gain (Loss) From Form 4797

 *Include only ordinary gains or losses from the sale, exchange, or involuntary conversion of assets used in a trade or business activity. Ordinary gains or losses from the sale, exchange, or involuntary conversion of rental activity assets are reported separately on line 19 of Form 8825 or line 3 of Schedules K and K-1, generally as a part of the net income (loss) from the rental activity.*

A partnership that is a partner in another partnership must include on **Form 4797**, Sales of Business Property,

its share of ordinary gains (losses) from sales, exchanges, or involuntary conversions (other than casualties or thefts) of the other partnership's trade or business assets.

Do not include any recapture of section 179 expense deduction. See the instructions for line 25, Supplemental Information, item 4, and the Instructions for Form 4797 for more information.

## Line 7—Other Income (Loss)


Enter on line 7 trade or business income (loss) that is not included on lines 1a through 6. Examples of such income include:

1. Interest income derived in the ordinary course of the partnership's trade or business, such as interest charged on receivable balances.
2. Recoveries of bad debts deducted in earlier years under the specific charge-off method.
3. Taxable income from insurance proceeds.
4. The amount of credit figured on **Form 6478**, Credit for Alcohol Used as Fuel.
5. All section 481 income adjustments resulting from changes in accounting methods. Show the computation of the section 481 adjustments on an attached schedule.
6. The amount of any deduction previously taken under section 179A that is subject to recapture. See **Pub. 535**, Business Expenses, for details, including how to figure the recapture.
7. The recapture amount for section 280F if the business use of listed property drops to 50% or less. To figure the recapture amount, the partnership must complete Part IV of Form 4797.

Do not include items requiring separate computations that must be reported on Schedules K and K-1. See the instructions for Schedules K and K-1 later in these instructions.

**Do not report portfolio or rental activity income (loss) on this line.**

## Deductions

 **Report only trade or business activity deductions on lines 9 through 21.**

**Do not** report the following expenses on lines 9 through 21:

- Rental activity expenses. Report these expenses on Form 8825 or line 3b of Schedule K.
- Deductions allocable to portfolio income. Report these deductions on line 10 of Schedules K and K-1.
- Nondeductible expenses (e.g., expenses connected with the production of tax-exempt income). Report nondeductible expenses on line 21 of Schedules K and K-1.
- Qualified expenditures to which an election under section 59(e) may apply. The instructions for lines 18a and 18b of Schedules K and K-1 explain how to report these amounts.

- Items the partnership must state separately that require separate computations by the partners. Examples include expenses incurred for the production of income instead of in a trade or business, charitable contributions, foreign taxes paid, intangible drilling and development costs, soil and water conservation expenditures, amortizable basis of reforestation expenditures, and exploration expenditures. The distributive shares of these expenses are reported separately to each partner on Schedule K-1.

## Limitations on Deductions

**Section 263A uniform capitalization rules.** The uniform capitalization rules of section 263A require partnerships to capitalize or include in inventory costs, certain costs incurred in connection with:

- The production of real and tangible personal property held in inventory or held for sale in the ordinary course of business.
- Real property or personal property (tangible and intangible) acquired for resale.
- The production of real property and tangible personal property by a partnership for use in its trade or business or in an activity engaged in for profit.

The costs required to be capitalized under section 263A are not deductible until the property to which the costs relate is sold, used, or otherwise disposed of by the partnership.

**Exceptions:** Section 263A does not apply to:

- Inventoriable items accounted for in the same manner as materials and supplies that are not incidental. See **Schedule A—Cost of Goods Sold** on page 19 for details.
- Personal property acquired for resale if the partnership's average annual gross receipts for the 3 prior tax years were \$10 million or less.
- Timber.
- Most property produced under a long-term contract.
- Certain property produced in a farming business. See the note at the end of the instructions for line 5.

The partnership must report the following costs separately to the partners for purposes of determinations under section 59(e):

- Research and experimental costs under section 174.
- Intangible drilling costs for oil, gas, and geothermal property.
- Mining exploration and development costs.

**Tangible personal property** produced by a partnership includes a film, sound recording, video tape, book, or similar property.

Partnerships subject to the rules are required to capitalize not only direct costs but an allocable part of most indirect costs (including taxes) that benefit the assets produced or acquired for resale, or are incurred by reason of the

performance of production or resale activities.

For inventory, some of the **indirect costs** that must be capitalized are:

- Administration expenses.
- Taxes.
- Depreciation.
- Insurance.
- Compensation paid to officers attributable to services.
- Rework labor.
- Contributions to pension, stock bonus, and certain profit-sharing, annuity, or deferred compensation plans.

Regulations section 1.263A-1(e)(3) specifies other indirect costs that relate to production or resale activities that must be capitalized and those that may be currently deductible.

Interest expense paid or incurred during the production period of designated property must be capitalized and is governed by special rules. For more details, see Regulations sections 1.263A-8 through 1.263A-15.

For more details on the uniform capitalization rules, see Regulations sections 1.263A-1 through 1.263A-3.

**Transactions between related taxpayers.** Generally, an accrual basis partnership may deduct business expenses and interest owed to a related party (including any partner) only in the tax year of the partnership that includes the day on which the payment is includible in the income of the related party. See section 267 for details.

**Business start-up expenses.** Business start-up expenses must be capitalized. An election may be made to amortize them over a period of not less than 60 months. See Pub. 535 and Regulations section 1.195-1.

**Organization costs.** Amounts paid or incurred to organize a partnership are capital expenditures. They are not deductible as a current expense.

The partnership may elect to amortize organization expenses over a period of 60 or more months, beginning with the month in which the partnership begins business. Include the amortization expense on line 20. On the balance sheet (Schedule L) show the unamortized balance of organization costs. See the instructions for line 10 for the treatment of organization expenses paid to a partner. See Pub. 535 for more information.

**Syndication costs.** Costs for issuing and marketing interests in the partnership, such as commissions, professional fees, and printing costs, must be capitalized. They cannot be depreciated or amortized. See the instructions for line 10 for the treatment of syndication fees paid to a partner.

**Reducing certain expenses for which credits are allowable.** For each of the following credits, the partnership must reduce the otherwise allowable deductions for expenses used to figure the credit by the amount of the current year credit:

1. The work opportunity credit.
2. The welfare-to-work credit.
3. The credit for increasing research activities.
4. The enhanced oil recovery credit.
5. The disabled access credit.
6. The empowerment zone and renewal community employment credit.
7. The Indian employment credit.
8. The credit for employer social security and Medicare taxes paid on certain employee tips.
9. The orphan drug credit.

If the partnership has any of these credits, figure each current year credit before figuring the deductions for expenses on which the credit is based.

## Line 9—Salaries and Wages

Enter on line 9 the salaries and wages paid or incurred for the tax year, reduced by any applicable employment credits from **Form 5884**, Work Opportunity Credit; **Form 8861**, Welfare-to-Work Credit; **Form 8844**, Empowerment Zone and Renewal Community Employment Credit; and **Form 8845**, Indian Employment Credit. See the instructions for these forms for more information.

Do not include salaries and wages reported elsewhere on the return, such as amounts included in cost of goods sold, elective contributions to a section 401(k) cash or deferred arrangement, or amounts contributed under a salary reduction SEP agreement or a SIMPLE IRA plan.

## Line 10—Guaranteed Payments to Partners

Deduct payments or credits to a partner for services or for the use of capital if the payments or credits are determined without regard to partnership income and are allocable to a trade or business activity. Also include on line 10 amounts paid during the tax year for insurance that constitutes medical care for a partner, a partner's spouse, or a partner's dependents.

Do not include any payments and credits that should be capitalized. For example, although payments or credits to a partner for services rendered in organizing or syndicating a partnership may be guaranteed payments, they are not deductible on line 10. They are capital expenditures. However, they should be separately reported on Schedules K and K-1, line 5.

Do not include distributive shares of partnership profits.

Report the guaranteed payments to the appropriate partners on Schedule K-1, line 5.

## Line 11—Repairs and Maintenance

Enter the costs of incidental repairs and maintenance that do not add to the value of the property or appreciably prolong its life, but only to the extent that such costs relate to a trade or business activity and are not claimed elsewhere on the return.



New buildings, machinery, or permanent improvements that increase the value of the property are not deductible. They are chargeable to capital accounts and may be depreciated or amortized.

### Line 12—Bad Debts

Enter the total debts that became worthless in whole or in part during the year, but only to the extent such debts relate to a trade or business activity. Report deductible nonbusiness bad debts as a short-term capital loss on Schedule D (Form 1065).



*Cash method partnerships cannot take a bad debt deduction unless the amount was previously included in income.*

### Line 13—Rent

Enter rent paid on business property used in a trade or business activity. Do not deduct rent for a dwelling unit occupied by any partner for personal use.

If the partnership rented or leased a vehicle, enter the total annual rent or lease expense paid or incurred in the trade or business activities of the partnership. Also complete Part V of **Form 4562**, Depreciation and Amortization. If the partnership leased a vehicle for a term of 30 days or more, the deduction for vehicle lease expense may have to be reduced by an amount called the **inclusion amount**. You may have an inclusion amount if:

**And the vehicle's FMV on the first day of the lease exceeded:**

<b>The lease term began:</b>	
After 12/31/98 . . . . .	\$15,500
After 12/31/96 but before 1/1/99 . . . . .	\$15,800
After 12/31/94 but before 1/1/97 . . . . .	\$15,500
If the lease term began before January 1, 1995, see <b>Pub. 463</b> , Travel, Entertainment, Gift, and Car Expenses, to find out if the partnership has an inclusion amount.	

See Pub. 463 for instructions on figuring the inclusion amount.

### Line 14—Taxes and Licenses

Enter taxes and licenses paid or incurred in the trade or business activities of the partnership if not reflected in cost of goods sold. Federal import duties and Federal excise and stamp taxes are deductible only if paid or incurred in carrying on the trade or business of the partnership.

**Do not** deduct the following taxes on line 14:

- State and local sales taxes paid or incurred in connection with the acquisition or disposition of business property. These taxes must be added to the cost of the property, or, in the case of a disposition, subtracted from the amount realized.
- Taxes assessed against local benefits to the extent that they increase the value

of the property assessed, such as for paving, etc.

- Federal income taxes or taxes reported elsewhere on the return.
- Section 901 foreign taxes. Report these taxes separately on Schedules K and K-1, line 17g.
- Taxes allocable to a rental activity. Taxes allocable to a rental real estate activity are reported on Form 8825. Taxes allocable to a rental activity other than a rental real estate activity are reported on line 3b of Schedule K.
- Taxes allocable to portfolio income. These taxes are reported on line 10 of Schedules K and K-1.
- Taxes paid or incurred for the production or collection of income, or for the management, conservation, or maintenance of property held to produce income. Report these taxes separately on line 11 of Schedules K and K-1.

See section 263A(a) for rules on capitalization of allocable costs (including taxes) for any property.

### Line 15—Interest

Include only interest incurred in the trade or business activities of the partnership that is not claimed elsewhere on the return.

Do not deduct interest expense on debt required to be allocated to the production of designated property. Designated property includes real property, personal property that has a class life of 20 years or more, and other tangible property requiring more than 2 years (1 year in the case of property with a cost of more than \$1 million) to produce or construct. Interest that is allocable to designated property produced by a partnership for its own use or for sale must be capitalized.

In addition, a partnership must also capitalize any interest on debt that is allocable to an asset used to produce designated property. A partner may be required to capitalize interest that was incurred by the partner for the partnership's production expenditures. Similarly, a partner may have to capitalize interest that was incurred by the partnership for the partner's own production expenditures. The information required by the partner to properly capitalize interest for this purpose must be provided by the partnership on an attachment for line 25 of Schedule K-1. See section 263A(f) and Regulations sections 1.263A-8 through 1.263A-15.

Do not include interest expense on debt used to purchase rental property or debt used in a rental activity. Interest allocable to a rental real estate activity is reported on Form 8825 and is used in arriving at net income (loss) from rental real estate activities on line 2 of Schedules K and K-1. Interest allocable to a rental activity other than a rental real estate activity is included on line 3b of Schedule K and is used in arriving at net income (loss) from a rental activity (other than a rental real estate activity). This net

amount is reported on line 3c of Schedule K and line 3 of Schedule K-1.

Do not include interest expense on debt used to buy property held for investment. Do not include interest expense that is clearly and directly allocable to interest, dividend, royalty, or annuity income not derived in the ordinary course of a trade or business. Interest paid or incurred on debt used to purchase or carry investment property is reported on line 14a of Schedules K and K-1. See the instructions for line 14a of Schedules K and K-1 and **Form 4952**, Investment Interest Expense Deduction, for more information on investment property.

Do not include interest on debt proceeds allocated to distributions made to partners during the tax year. Instead, report such interest on line 11 of Schedules K and K-1. To determine the amount to allocate to distributions to partners, see Notice 89-35, 1989-1 C.B. 675.

Temporary Regulations section 1.163-8T gives rules for allocating interest expense among activities so that the limitations on passive activity losses, investment interest, and personal interest can be properly figured. Generally, interest expense is allocated in the same manner that debt is allocated. Debt is allocated by tracing disbursements of the debt proceeds to specific expenditures, as provided in the regulations.

Interest paid by a partnership to a partner for the use of capital should be entered on line 10 as guaranteed payments.

Prepaid interest can only be deducted over the period to which the prepayment applies.

**Note:** *Additional limitations on interest deductions apply when the partnership is a policyholder or beneficiary with respect to a life insurance, endowment, or annuity contract issued after June 8, 1997. For details, see section 264. Attach a statement showing the computation of the deduction disallowed under section 264.*

### Line 16—Depreciation

On line 16a, enter **only** the depreciation claimed on assets used in a trade or business activity. Enter on line 16b the depreciation reported elsewhere on the return (for example, on Schedule A) that is attributable to assets used in trade or business activities. See the Instructions for Form 4562 or **Pub. 946**, How To Depreciate Property, to figure the amount of depreciation to enter on this line.

For depreciation, you must complete and attach Form 4562 only if the partnership placed property in service during the tax year or claims depreciation on any car or other listed property.

Do not include any section 179 expense deduction on this line. This amount is not deducted by the partnership. Instead, it is passed through to the partners on line 9 of Schedule K-1.



## Line 17—Depletion

If the partnership claims a deduction for timber depletion, complete and attach **Form T**, Forest Activities Schedules.



*Do not deduct depletion for oil and gas properties. Each partner figures depletion on oil and gas properties. See the instructions for Schedule K-1, line 25, item 3, for the information on oil and gas depletion that must be supplied to the partners by the partnership.*

## Line 18—Retirement Plans, etc.

Do not deduct payments for partners to retirement or deferred compensation plans including IRAs, qualified plans, and simplified employee pension (SEP) and SIMPLE IRA plans on this line. These amounts are reported on Schedule K-1, line 11, and are deducted by the partners on their own returns.

Enter the deductible contributions not claimed elsewhere on the return made by the partnership for its common-law employees under a qualified pension, profit-sharing, annuity, or SEP or SIMPLE IRA plan, and under any other deferred compensation plan.

If the partnership contributes to an individual retirement arrangement (IRA) for employees, include the contribution in salaries and wages on page 1, line 9, or Schedule A, line 3, and not on line 18.

Employers who maintain a pension, profit-sharing, or other funded deferred compensation plan (other than a SEP or SIMPLE IRA), whether or not the plan is qualified under the Internal Revenue Code and whether or not a deduction is claimed for the current year, generally must file the applicable form listed below:

- **Form 5500**, Annual Return/Report of Employee Benefit Plan. File this form for a plan that is not a one-participant plan (see below).
- **Form 5500-EZ**, Annual Return of One-Participant (Owners and Their Spouses) Retirement Plan. File this form for a plan that only covers one or more partners (or partners and their spouses).

There are penalties for not filing these forms on time.

## Line 19—Employee Benefit Programs

Enter the partnership's contributions to employee benefit programs not claimed elsewhere on the return (for example, insurance, health, and welfare programs) that are not part of a pension, profit-sharing, etc., plan included on line 18.

Do not include amounts paid during the tax year for insurance that constitutes medical care for a partner, a partner's spouse, or a partner's dependents. Instead, include these amounts on line 10 as guaranteed payments and on Schedule K, line 5, and Schedule K-1, line 5, of each partner on whose behalf the amounts were paid. Also report these amounts on Schedule K, line 11, and

Schedule K-1, line 11, of each partner on whose behalf the amounts were paid.

## Line 20—Other Deductions

Attach your own schedule listing by type and amount all allowable deductions related to a trade or business activity **only** for which there is no separate line on page 1 of Form 1065. Enter the total on this line. Examples of other deductions include:

- Amortization (except as noted below)—see the Instructions for Form 4562 for more information. Complete and attach Form 4562 if the partnership is claiming amortization of costs that began during the tax year.
- Insurance premiums.
- Legal and professional fees.
- Supplies used and consumed in the business.
- Utilities.
- Part of the cost of qualified clean-fuel vehicle property and qualified clean-fuel vehicle refueling property. For more details, see section 179A.

Also, see **Special Rules** below for limits on certain other deductions.

**Do not** deduct on line 20:

- Items that must be reported separately on Schedules K and K-1.
- Qualified expenditures to which an election under section 59(e) may apply. See the instructions on page 29 for lines 18a and 18b of Schedule K-1 for details on treatment of these items.
- Amortization of reforestation expenditures under section 194. The partnership can elect to amortize up to \$10,000 of qualified reforestation expenditures paid or incurred during the tax year. However, the amortization is not deducted by the partnership but the amortizable basis is instead separately allocated among the partners. See the instructions on page 31 for Schedule K-1, line 25, item 21 and Pub. 535 for more details.
- Fines or penalties paid to a government for violating any law. Report these expenses on Schedule K, line 21.
- Expenses allocable to tax-exempt income. Report these expenses on Schedule K, line 21.
- Net operating losses. Only individuals and corporations may claim a net operating loss deduction.
- Amounts paid or incurred to participate or intervene in any political campaign on behalf of a candidate for public office, or to influence the general public regarding legislative matters, elections, or referendums. Report these expenses on Schedule K, line 21.
- Expenses paid or incurred to influence Federal or state legislation, or to influence the actions or positions of certain Federal executive branch officials. However, certain in-house lobbying expenditures that do not exceed \$2,000 are deductible. See section 162(e) for more details.

## Special Rules

**Commercial revitalization deduction.** If the partnership constructs, purchases, or substantially rehabilitates a qualified

building in a renewal community it may qualify for a deduction of either **(a)** 50% of qualified capital expenditures in the year the building is placed in service or **(b)** amortization of 100% of the qualified capital expenditures over a 120-month period beginning with the month the building is placed in service. If the partnership elects to amortize these expenditures, complete and attach Form 4562. To qualify, the building must be nonresidential (as defined in section 168(e)(2)) and placed in service by the partnership. The partnership must be the original user of the building unless it is substantially rehabilitated. The amount of the qualified expenditures cannot exceed the lesser of \$10 million or the amount allocated to the building by the commercial revitalization agency of the state in which the building is located. Any remaining expenditures are depreciated over the regular depreciation recovery period. See **Pub. 954**, Tax Incentives for Empowerment Zones and Other Distressed Communities, and section 1400I for details.

**Rental real estate.** Do not report this deduction on line 20 if the building is placed in service as rental real estate. A commercial revitalization deduction for rental real estate is not deducted by the partnership but is passed through to the partners on line 25 of Schedule K-1.

## Travel, meals, and entertainment.

Subject to limitations and restrictions discussed below, a partnership can deduct ordinary and necessary travel, meals, and entertainment expenses paid or incurred in its trade or business. Special rules apply to deductions for gifts, skybox rentals, luxury water travel, convention expenses, and entertainment tickets. See section 274 and Pub. 463 for more details.

**Travel.** The partnership cannot deduct travel expenses of any individual accompanying a partner or partnership employee, including a spouse or dependent of the partner or employee, unless:

- That individual is an employee of the partnership and
- His or her travel is for a bona fide business purpose and would otherwise be deductible by that individual.

## Meals and entertainment.

Generally, the partnership can deduct only 50% of the amount otherwise allowable for meals and entertainment expenses. In addition (subject to exceptions under section 274(k)(2)):

- Meals must not be lavish or extravagant,
- A bona fide business discussion must occur during, immediately before, or immediately after the meal, and
- A partner or employee of the partnership must be present at the meal.

See section 274(n)(3) for a special rule that applies to expenses for meals consumed by individuals subject to the hours of service limits of the Department of Transportation.

**Membership dues.** The partnership may deduct amounts paid or incurred for membership dues in civic or public service organizations, professional organizations (such as bar and medical associations), business leagues, trade associations, chambers of commerce, boards of trade, and real estate boards. However, no deduction is allowed if a principal purpose of the organization is to entertain, or provide entertainment facilities for, members or their guests. In addition, the partnership may not deduct membership dues in any club organized for business, pleasure, recreation, or other social purpose. This includes country clubs, golf and athletic clubs, airline and hotel clubs, and clubs operated to provide meals under conditions favorable to business discussion.

**Entertainment facilities.** The partnership cannot deduct an expense paid or incurred for a facility (such as a yacht or hunting lodge) used for an activity usually considered entertainment, amusement, or recreation.

**Note:** *The partnership may be able to deduct otherwise nondeductible meals, travel, and entertainment expenses if the amounts are treated as compensation and reported on Form W-2 for an employee or on Form 1099-MISC for an independent contractor.*

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## Schedule A—Cost of Goods Sold

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### Cost of Goods Sold

Generally, inventories are required at the beginning and end of each tax year if the production, purchase, or sale of merchandise is an income-producing factor. See Regulations section 1.471-1.

However, if the partnership is a qualifying taxpayer or a qualifying small business taxpayer, it may adopt or change its accounting method to account for inventoriable items in the same manner as materials and supplies that are not incidental.

A **qualifying taxpayer** is a taxpayer (a) whose average annual gross receipts for the 3 prior tax years are \$1 million or less and (b) whose business is not a tax shelter (as defined in section 448(d)(3)).

A **qualifying small business taxpayer** is a taxpayer (a) whose average annual gross receipts for the 3 prior tax years are more than \$1 million but not more than \$10 million, (b) whose business is not a tax shelter (as defined in section 448(d)(3)), and (c) whose principal business activity is not an ineligible activity as explained in Rev. Proc. 2002-28.

Under this accounting method, inventory costs for raw materials purchased for use in producing finished goods and merchandise purchased for resale are deductible in the year the

finished goods or merchandise are sold (but not before the year the partnership paid for the raw materials or merchandise, if it is also using the cash method). Enter amounts paid for all raw materials and merchandise during the tax year on line 2. The amount the partnership can deduct for the tax year is figured on line 8. For additional guidance on this method of accounting for inventory items, see Rev. Proc. 2001-10, 2001-2 I.R.B. 272 if you are a qualifying taxpayer or Rev. Proc. 2002-28 if you are a qualifying small business taxpayer.

All filers that have not elected to treat inventoriable items as materials and supplies that are not incidental should see **Section 263A uniform capitalization rules** on page 16 before completing Schedule A. The instructions below for lines 2 through 9 apply to Schedule A.

### Line 1—Inventory at Beginning of Year

If the partnership is changing its method of accounting for the current tax year, it must refigure last year's closing inventory using its new method of accounting and enter the result on line 1. If there is a difference between last year's closing inventory and the refigured amount, attach an explanation and take it into account when figuring the partnership's section 481(a) adjustment (explained on page 6).

### Line 2—Purchases

Reduce purchases by items withdrawn for personal use. The cost of these items should be shown on line 23 of Schedules K and K-1 as distributions to partners.

### Line 4—Additional Section 263A Costs

An entry is required on this line only for partnerships that have elected a simplified method.

For partnerships that have elected the **simplified production method**, additional section 263A costs are generally those costs, other than interest, that were not capitalized under the partnership's method of accounting immediately prior to the effective date of section 263A that are required to be capitalized under section 263A. Interest must be accounted for separately. For new partnerships, additional section 263A costs are the costs, other than interest, that must be capitalized under section 263A, but which the partnership would not have been required to capitalize if it had existed before the effective date of section 263A. For more details, see Regulations section 1.263A-2(b).

For partnerships that have elected the **simplified resale method**, additional section 263A costs are generally those costs incurred with respect to the following categories:

- Off-site storage or warehousing.
- Purchasing.
- Handling, such as processing, assembly, repackaging, and transporting.

- General and administrative costs (mixed service costs). For more details, see Regulations section 1.263A-3(d).

Enter on line 4 the balance of section 263A costs paid or incurred during the tax year not includable on lines 2, 3, and 5. Attach a schedule listing these costs.

### Line 5—Other Costs

Enter on line 5 any other inventoriable costs paid or incurred during the tax year not entered on lines 2 through 4. Attach a schedule.

### Line 7—Inventory at End of Year

See Regulations sections 1.263A-1 through 1.263A-3 for details on figuring the amount of additional section 263A costs to be included in ending inventory.

If the partnership accounts for inventoriable items in the same manner as materials and supplies that are not incidental, enter on line 7 the portion of its raw materials and merchandise purchased for resale that are included on line 6 and were not sold during the year. See Rev. Proc. 2001-10 and Rev. Proc. 2002-28 for more information.

### Lines 9a through 9c—Inventory Valuation Methods

Inventories can be valued at:

- Cost,
- Cost or market value (whichever is lower), or
- Any other method approved by the IRS that conforms to the requirements of the applicable regulations.

However, the partnership is required to use cost if it is using the cash method of accounting.

Partnerships that account for inventoriable items in the same manner as materials and supplies that are not incidental may currently deduct expenditures for direct labor and all indirect costs that would otherwise be included in inventory costs. See Rev. Proc. 2001-10 and Rev. Proc. 2002-28 for more information.

The average cost (rolling average) method of valuing inventories generally does not conform to the requirements of the regulations. See Rev. Rul. 71-234, 1971-1 C.B. 148.

Partnerships that use erroneous valuation methods must change to a method permitted for Federal tax purposes. To make this change, use Form 3115.

On line 9a, check the methods used for valuing inventories. Under lower of cost or market, the term "market" (for normal goods) means the current bid price prevailing on the inventory valuation date for the particular merchandise in the volume usually purchased by the taxpayer. For a manufacturer, market applies to the basic elements of cost—raw materials, labor, and burden. If section 263A applies to the taxpayer, the basic elements of cost must reflect the current bid price of all direct costs and all



indirect costs properly allocable to goods on hand at the inventory date.

Inventory may be valued below cost when the merchandise is unsalable at normal prices or unusable in the normal way because the goods are subnormal due to damage, imperfections, shop wear, etc., within the meaning of Regulations section 1.471-2(c). These goods may be valued at the current bona fide selling price minus the direct cost of disposition (but not less than scrap value) if such a price can be established.

If this is the first year the last-in first-out (LIFO) inventory method was either adopted or extended to inventory goods not previously valued under the LIFO method, attach **Form 970**, Application To Use LIFO Inventory Method, or a statement with the information required by Form 970. Also check the box on line 9c.

If the partnership has changed or extended its inventory method to LIFO and has had to write up its opening inventory to cost in the year of election, report the effect of this write-up as income (line 7, page 1, Form 1065) proportionately over a 3-year period that begins in the tax year of the LIFO election.

For more information on inventory valuation methods, see **Pub. 538**, Accounting Periods and Methods.

## Schedule B—Other Information

### Question 1

Check box 1(f) for any other type of entity and state the type.

### Question 3

The partnership must answer **Yes** to Question 3, if during the tax year, it owned:

- An interest in another partnership (foreign or domestic) or
- A foreign entity that was disregarded as an entity separate from the partnership under Regulations sections 301.7701-2 and 301.7701-3.

If the partnership answered **Yes** to this question, report the following information on an attached schedule:

1. If the partnership owned at least a 10% interest, directly or indirectly, in any other foreign or domestic partnership (other than any partnership for which a Form 8865 is attached to the tax return), show each partnership's name, EIN (if any), and the country under whose laws the partnership was organized.

2. If the partnership owned any entities that have been disregarded as separate from the partnership, show each disregarded entity's name, EIN (if any), and the country under whose laws the entity was organized.

**Note:** For each entity listed on the attached schedule, clearly indicate

*whether the entity is a partnership or a disregarded entity.*

### Question 4—Consolidated Audit Procedures

Generally, the tax treatment of partnership items is determined at the partnership level in a consolidated audit proceeding, rather than in separate proceedings with individual partners.

Answer **Yes** to Question 4 if **any** of the following apply:

- The partnership had more than 10 partners at any one time during the tax year. For purposes of this question, a husband and wife, and their estates, count as one person.
- Any partner was a nonresident alien or was other than an individual, an estate, or a C corporation.
- The partnership is a "small partnership" that has elected to be subject to the rules for consolidated audit proceedings. "Small partnerships" as defined in section 6231(a)(1)(B)(i) are not subject to the rules for consolidated audit proceedings unless an election to be covered by them is made under Regulations section 301.6231(a)(1)-1(b)(2). Once made, the election may not be revoked without IRS consent.



*The partnership does not make this election when it answers **Yes** to Question 4. The election must be made separately.*

If a partnership return is filed by an entity for a tax year, but it is determined that the entity is not a partnership for that tax year, the consolidated partnership audit procedures will generally apply to that entity and to persons holding an interest in that entity. See Regulations section 301.6233-1 for details and exceptions.

### Question 5

Answer **Yes** to Question 5 if the partnership meets all three of the requirements shown on the form. Total receipts is defined as the sum of gross receipts or sales (page 1, line 1a); all other income (page 1, lines 4 through 7); income reported on Schedule K, lines 3a, 4a, 4b, and 4c; income or net gain reported on Schedule K, lines 4d, 4e(1), 4f, 6, and 7; and income or net gain reported on Form 8825, lines 2, 19, and 20a.

### Question 6—Foreign Partners

Answer **Yes** to Question 6 if the partnership had any foreign partners (for purposes of section 1446) at any time during the tax year. Otherwise, answer **No**.

If the partnership had gross income effectively connected with a trade or business in the United States **and** foreign partners, it may be required to withhold tax under section 1446 on income allocable to foreign partners (without regard to distributions) and file Forms 8804, 8805, and 8813. See Rev. Proc. 89-31, 1989-1 C.B. 895 and Rev. Proc.

92-66, 1992-2 C.B. 428 for more information.

### Question 7

Answer **Yes** to Question 7 if interests in the partnership are traded on an established securities market or are readily tradable on a secondary market (or its substantial equivalent).

### Question 8

Organizers of certain tax shelters are required to register the tax shelters by filing **Form 8264**, Application for Registration of a Tax Shelter, no later than the day on which an interest in the shelter is first offered for sale. Organizers filing a properly completed Form 8264 will receive a tax shelter registration number that they must furnish to their investors. See the Instructions for Form 8264 for the definition of a tax shelter and the investments exempted from tax shelter registration.

### Question 9—Foreign Accounts

Answer **Yes** to Question 9 if either **1** or **2** below applies to the partnership. Otherwise, check the **No** box.

1. At any time during calendar year 2002, the partnership had an interest in or signature or other authority over a bank account, securities account, or other financial account in a foreign country; **and**
  - The combined value of the accounts was more than \$10,000 at any time during the calendar year; **and**
  - The accounts were **not** with a U.S. military banking facility operated by a U.S. financial institution.
2. The partnership owns more than 50% of the stock in any corporation that would answer the question **Yes** based on item **1** above.

Get **Form TD F 90-22.1**, Report of Foreign Bank and Financial Accounts, to see if the partnership is considered to have an interest in or signature or other authority over a bank account, securities account, or other financial account in a foreign country.

If you answered **Yes** to Question 9, file Form TD F 90-22.1 by June 30, 2003, with the Department of the Treasury at the address shown on the form. Because Form TD F 90-22.1 is not a tax return, **do not** file it with Form 1065. You may order Form TD F 90-22.1 by calling 1-800-829-3676.

### Question 10

The partnership may be required to file **Form 3520**, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, if:

- It directly or indirectly transferred property or money to a foreign trust. For this purpose, any U.S. person who created a foreign trust is considered a transferor.
- It is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.
- It received a distribution from a foreign trust.

For more information, see the Instructions for Form 3520.

**Note:** An owner of a foreign trust must ensure that the trust files an annual information return on **Form 3520-A**, Annual Information Return of Foreign Trust with a U.S. Owner.

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## Designation of Tax Matters Partner (TMP)

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If the partnership is subject to the rules for consolidated audit proceedings in sections 6221 through 6233, the partnership may designate a partner as the TMP for the tax year for which the return is filed by completing the **Designation of Tax Matters Partner** section on page 2 of Form 1065. See the instructions for Question 4, consolidated audit procedures, to determine if the partnership is subject to these rules. The designated TMP must be a general partner and, in most cases, must also be a U.S. person. For details, see Regulations section 301.6231(a)(7)-1.

For a limited liability company (LLC), only a member-manager of the LLC is treated as a general partner. A member-manager is any owner of an interest in the LLC who, alone or together with others, has the continuing exclusive authority to make the management decisions necessary to conduct the business for which the LLC was formed. If there are no elected or designated member-managers, each owner is treated as a member-manager. For details, see Regulations section 301.6231(a)(7)-2.

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## Schedules K and K-1 — Partners' Shares of Income, Credits, Deductions, etc.

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### Purpose of Schedules

Although the partnership is not subject to income tax, the partners are liable for tax on their shares of the partnership income, whether or not distributed, and must include their shares on their tax returns.

**Schedule K** (page 3 of Form 1065) is a summary schedule of all the partners' shares of the partnership's income, credits, deductions, etc. All partnerships must complete Schedule K. Rental activity income (loss) and portfolio income are not reported on page 1 of Form 1065. These amounts are not combined with trade or business activity income (loss). Schedule K is used to report the totals of these and other amounts.

**Schedule K-1** (Form 1065) shows each partner's separate share. Attach a copy of each Schedule K-1 to the Form 1065 filed with the IRS; keep a copy with a copy of the partnership return as a part of the partnership's records; and furnish a copy

to each partner. If a partnership interest is held by a nominee on behalf of another person, the partnership may be required to furnish Schedule K-1 to the nominee. See Temporary Regulations sections 1.6031(b)-1T and 1.6031(c)-1T for more information.

Give each partner a copy of either the Partner's Instructions for Schedule K-1 (Form 1065) or specific instructions for each item reported on the partner's Schedule K-1 (Form 1065).

### Substitute Forms

The partnership does not need IRS approval to use a substitute Schedule K-1 if it is an exact copy of the IRS schedule, or if it contains only those lines the taxpayer is required to use. The lines must use the same numbers and titles and must be in the same order and format as on the comparable IRS Schedule K-1. The substitute schedule must include the OMB number. The partnership must provide each partner with the Partner's Instructions for Schedule K-1 (Form 1065) or other prepared specific instructions.

The partnership must request IRS approval to use other substitute Schedules K-1. To request approval, write to Internal Revenue Service, Attention: Substitute Forms Program, W:CAR:MP:FP:S:SP, 1111 Constitution Avenue, NW, Washington, DC 20224.

Each partner's information must be on a separate sheet of paper. Therefore, separate all continuously printed substitutes before you file them with the IRS.

The partnership may be subject to a penalty if it files Schedules K-1 that do not conform to the specifications of Rev. Proc. 2002-60, 2002-40 I.R.B. 645.

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## How Income Is Shared Among Partners

Allocate shares of income, gain, loss, deduction, or credit among the partners according to the partnership agreement for sharing income or loss generally. Partners may agree to allocate specific items in a ratio different from the ratio for sharing income or loss. For instance, if the net income exclusive of specially allocated items is divided evenly among three partners but some special items are allocated 50% to one, 30% to another, and 20% to the third partner, report the specially allocated items on the appropriate line of the applicable partner's Schedule K-1 and the total on the appropriate line of Schedule K, instead of on the numbered lines on page 1 of Form 1065 or Schedules A or D.

If a partner's interest changed during the year, see section 706(d) before determining each partner's distributive share of any item of income, gain, loss, deduction, etc. Income (loss) is allocated to a partner only for the part of the year in which that person is a member of the partnership. The partnership will either allocate on a daily basis or divide the partnership year into segments and allocate income, loss, or special items in

each segment among the persons who were partners during that segment. Partnerships that report their income on the cash basis must allocate interest expense, taxes, and any payment for services or for the use of property on a daily basis if there is any change in any partner's interest during the year. See Pub. 541 for more details.

Special rules on the allocation of income, gain, loss, and deductions generally apply if a partner contributes property to the partnership and the FMV of that property at the time of contribution differs from the contributing partner's adjusted tax basis. Under these rules, the partnership must use a reasonable method of making allocations of income, gain, loss, and deductions from the property so that the contributing partner receives the tax burdens and benefits of any built-in gain or loss (i.e., pre-contribution appreciation or diminution of value of the contributed property). See Regulations section 1.704-3 for details on how to make these allocations, including a description of specific allocation methods that are generally reasonable.

See **Dispositions of Contributed Property** on page 9 for special rules on the allocation of income, gain, loss, and deductions on the disposition of property contributed to the partnership by a partner.

If the partnership agreement does not provide for the partner's share of income, gain, loss, deduction, or credit, or if the allocation under the agreement does not have substantial economic effect, the partner's share is determined according to the partner's interest in the partnership. See Regulations section 1.704-1 for more information.

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## Specific Instructions (Schedule K-1 Only)

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### General Information

Generally, the partnership is required to prepare and give a Schedule K-1 to each person who was a partner in the partnership at any time during the year. **Schedule K-1 must be provided to each partner on or before the day on which the partnership return is required to be filed.**

However, if a foreign partnership meets each of the following four requirements, it is not required to file or provide Schedules K-1 for foreign partners (unless the foreign partner is a passthrough entity through which a U.S. person holds an interest in the foreign partnership):

- The partnership had no gross income effectively connected with the conduct of a trade or business within the United States during its tax year.
- All required Forms 1042 and 1042-S were filed by the partnership or another withholding agent as required by Regulations section 1.1461-1(b) and (c).



- The tax liability for each foreign partner for amounts reportable under Regulations sections 1.1461-1(b) and (c) has been fully satisfied by the withholding of tax at the source.
- The partnership is not a withholding foreign partnership as defined in Regulations section 1.1441-5(c)(2)(i).

Generally, any person who holds an interest in a partnership as a nominee for another person must furnish to the partnership the name, address, etc., of the other person.

On each Schedule K-1, enter the names, addresses, and identifying numbers of the partner and partnership and the partner's distributive share of each item.

For an individual partner, enter the partner's social security number (SSN) or individual taxpayer identification number (ITIN). For all other partners, enter the partner's EIN. However, if a partner is an individual retirement arrangement (IRA), enter the identifying number of the custodian of the IRA. Do not enter the SSN of the person for whom the IRA is maintained.

Foreign partners without a U.S. taxpayer identifying number should be notified by the partnership of the necessity of obtaining a U.S. identifying number. Certain aliens who are not eligible to obtain SSNs can apply for an ITIN on **Form W-7**, Application for IRS Individual Taxpayer Identification Number.

If a husband and wife each had an interest in the partnership, prepare a separate Schedule K-1 for each of them. If a husband and wife held an interest together, prepare one Schedule K-1 if the two of them are considered to be one partner.

There is space on line 25 of Schedule K-1 for you to provide information to the partners. This space may be used instead of attachments.

## Specific Items and Questions

### Question A

Answer Question A on all Schedules K-1. If a partner holds interests as both a general and limited partner, check the first two boxes and attach a schedule for each activity that shows the amounts allocable to the partner's interest as a limited partner.

### Question B—What Type of Entity Is This Partner?

State on this line whether the partner is an individual, a corporation, an estate, a trust, a partnership, an exempt organization, or a nominee (custodian). If the partner is a nominee, use one of the following codes to indicate the type of entity the nominee represents: I—Individual; C—Corporation; F—Estate or Trust; P—Partnership; E—Exempt Organization; or IRA—Individual Retirement Arrangement.

### Question C—Domestic/Foreign Partner

Check the foreign partner box if the partner is a nonresident alien individual, foreign partnership, foreign corporation, or a foreign estate or trust. Otherwise, check the domestic partner box.

### Item D—Partner's Profit, Loss, and Capital Sharing Percentages

Enter in Item D, column (ii), the appropriate percentages as of the end of the year. However, if a partner's interest terminated during the year, enter in column (i) the percentages that existed immediately before the termination. When the profit or loss sharing percentage has changed during the year, show the percentage before the change in column (i) and the end-of-year percentage in column (ii). If there are multiple changes in the profit and loss sharing percentage during the year, attach a statement giving the date and percentage before each change.

"Ownership of capital" means the portion of the capital that the partner would receive if the partnership was liquidated at the end of the year by the distribution of undivided interests in partnership assets and liabilities.

### Item F—Partner's Share of Liabilities

Enter each partner's share of nonrecourse liabilities, partnership-level qualified nonrecourse financing, and other liabilities.

"Nonrecourse liabilities" are those liabilities of the partnership for which no partner bears the economic risk of loss. The extent to which a partner bears the economic risk of loss is determined under the rules of Regulations section 1.752-2. Do not include partnership-level qualified nonrecourse financing (defined below) on the line for nonrecourse liabilities.

If the partner terminated his or her interest in the partnership during the year, enter the share that existed immediately before the total disposition. In all other cases, enter it as of the end of the year.

If the partnership is engaged in two or more different types of at-risk activities, or a combination of at-risk activities and any other activity, attach a statement showing the partner's share of nonrecourse liabilities, partnership-level qualified nonrecourse financing, and other liabilities for **each** activity. See **Pub. 925**, Passive Activity and At-Risk Rules, to determine if the partnership is engaged in more than one at-risk activity.

The at-risk rules of section 465 generally apply to any activity carried on by the partnership as a trade or business or for the production of income. These rules generally limit the amount of loss and other deductions a partner can claim from any partnership activity to the amount for which that partner is considered at risk. However, for partners who acquired their partnership interests before 1987, the at-risk rules do not apply

to losses from an activity of holding real property the partnership placed in service before 1987. The activity of holding mineral property does not qualify for this exception. Identify on an attachment to Schedule K-1 the amount of any losses that are not subject to the at-risk rules.

If a partnership is engaged in an activity subject to the limitations of section 465(c)(1) (such as, films or videotapes, leasing section 1245 property, farming, or oil and gas property), give each partner his or her share of the total pre-1976 losses from that activity for which there existed a corresponding amount of nonrecourse liability at the end of each year in which the losses occurred. See **Form 6198**, At-Risk Limitations, and related instructions for more information.

Qualified nonrecourse financing secured by real property used in an activity of holding real property that is subject to the at-risk rules is treated as an amount at risk. "Qualified nonrecourse financing" generally includes financing for which no one is personally liable for repayment that is borrowed for use in an activity of holding real property and that is loaned or guaranteed by a Federal, state, or local government or that is borrowed from a "qualified" person. Qualified persons include any person actively and regularly engaged in the business of lending money, such as a bank or savings and loan association. Qualified persons generally do not include related parties (unless the nonrecourse financing is commercially reasonable and on substantially the same terms as loans involving unrelated persons), the seller of the property, or a person who receives a fee for the partnership's investment in the real property. See section 465 for more information on qualified nonrecourse financing.

The partner as well as the partnership must meet the qualified nonrecourse rules. Therefore, the partnership must enter on an attached statement any other information the partner needs to determine if the qualified nonrecourse rules are also met at the partner level.

### Item G—Tax Shelter Registration Number

If the partnership is a registration-required tax shelter or has invested in a registration-required tax shelter, it must enter the tax shelter registration number in Item G. Also, a partnership that has invested in a registration-required tax shelter must furnish a copy of its Form 8271 to its partners. See Form 8271 for more details.

### Item J—Analysis of Partner's Capital Account

You are not required to complete Item J if the answer to Question 5 of Schedule B is **Yes**. If you are required to complete this item, see the instructions for Schedule M-2 on page 32.

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## Specific Instructions (Schedules K and K-1, Except as Noted)

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Schedules K and K-1 have the same line numbers for lines 1 through 23.

### Special Allocations

An item is specially allocated if it is allocated to a partner in a ratio different from the ratio for sharing income or loss generally.

Report specially allocated ordinary gain (loss) on Schedules K and K-1, line 7. Report other specially allocated items on the applicable lines of the partner's Schedule K-1, with the total amount on the applicable line of Schedule K. For example, specially allocated long-term capital gain is entered on line 4e(1) of the partner's Schedule K-1, and the total is entered on line 4e(1) of Schedule K, along with any net long-term capital gain (or loss) from line 12(f) of Schedule D (Form 1065).

### Income (Loss)

#### Line 1—Ordinary Income (Loss) From Trade or Business Activities

Enter the amount from page 1, line 22. Enter the income (loss) without reference to (a) the basis of the partners' interests in the partnership, (b) the partners' at-risk limitations, or (c) the passive activity limitations. These limitations, if applicable, are determined at the partner level.

If the partnership has more than one trade or business activity, identify on an attachment to Schedule K-1 the amount from each separate activity. See **Passive Activity Reporting Requirements** on page 13.

Line 1 should not include rental activity income (loss) or portfolio income (loss).

#### Line 2—Net Income (Loss) From Rental Real Estate Activities

Enter the net income (loss) from rental real estate activities of the partnership from Form 8825. Attach this form to Form 1065. If the partnership has more than one rental real estate activity, identify on an attachment to Schedule K-1 the amount attributable to each activity.

#### Line 3—Net Income (Loss) From Other Rental Activities

On Schedule K, line 3a, enter gross income from rental activities other than those reported on Form 8825. See page 10 of these instructions and Pub. 925 for the definition of rental activities. Include on line 3a, the gain (loss) from line 18 of Form 4797 that is attributable to the sale, exchange, or involuntary conversion of an asset used in a rental activity other than a rental real estate activity.

On line 3b of Schedule K, enter the deductible expenses of the activity. Attach a schedule of these expenses to Form 1065.

Enter the net income (loss) on line 3c of Schedule K. Enter each partner's share on line 3 of Schedule K-1.

If the partnership has more than one rental activity reported on line 3, identify on an attachment to Schedule K-1 the amount from each activity.

#### Lines 4a Through 4f—Portfolio Income (Loss)

Enter portfolio income (loss) on lines 4a through 4f.

See page 11 of these instructions for a definition of portfolio income. Do not reduce portfolio income by deductions allocable to it. Report such deductions (other than interest expense) on line 10 of Schedules K and K-1. Interest expense allocable to portfolio income is generally investment interest expense and is reported on line 14a of Schedules K and K-1.

**Lines 4a and 4b.** Enter only taxable interest and ordinary dividends on these lines. Taxable interest is interest from all sources except interest exempt from tax and interest on tax-free covenant bonds.

**Lines 4d, 4e(1), 4e(2), and 4e(3).** Enter on line 4d of Schedule K the gain or loss from line 5 of Schedule D (Form 1065) plus any short-term capital gain (loss) that is specially allocated to partners. Report each partner's share on line 4d of Schedule K-1.

Enter on line 4e(1) the gain or loss from line 12 of Schedule D (Form 1065) plus any long-term capital gain (loss) that is specially allocated to partners. Enter on line 4e(2) the gain or loss from line 11 of Schedule D (Form 1065). Enter on line 4e(3) the gains (not losses) from the disposition of assets (excluding stock that could qualify for section 1202 gain) held more than 5 years that are portfolio income included on line 12 of Schedule D.



*If any gain or loss from line 5, 11, or 12 of Schedule D is from the disposition of nondepreciable personal property used in a trade or business, it may not be treated as portfolio income. Report such gain or loss on line 7 of Schedules K and K-1.*

**Line 4f.** Report and identify other portfolio income or loss on an attachment for line 4f.

For example, income reported to the partnership from a real estate mortgage investment conduit (REMIC), in which the partnership is a residual interest holder, would be reported on an attachment for line 4f. If the partnership holds a residual interest in a REMIC, report on the attachment for line 4f the partner's share of the following:

- Taxable income (net loss) from the REMIC (line 1b of Schedules Q (Form 1066)).
- "Excess inclusion" (line 2c of Schedules Q (Form 1066)).
- Section 212 expenses (line 3b of Schedules Q (Form 1066)). Do not report these section 212 expenses on line 10 of Schedules K and K-1.

Because Schedule Q (Form 1066) is a quarterly statement, the partnership must follow the Schedule Q instructions to figure the amounts to report to the partner for the partnership's tax year.

#### Line 5—Guaranteed Payments to Partners

Guaranteed payments to partners include:

- Payments for salaries, health insurance, and interest deducted by the partnership and reported on Form 1065, page 1, line 10; Form 8825; or on Schedule K, line 3b; and
- Payments the partnership must capitalize. See the Instructions for Form 1065, line 10.

Generally, amounts reported on line 5 are not considered to be related to a passive activity. For example, guaranteed payments for personal services paid to a partner would not be passive activity income. Likewise, interest paid to any partner is not passive activity income.

#### Line 6—Net Section 1231 Gain (Loss) (Other Than Due to Casualty or Theft)

Enter on line 6 the net section 1231 gain (loss) from Form 4797, line 7, column (g). Do not include specially allocated ordinary gains and losses or net gains or losses from involuntary conversions due to casualties or thefts on this line. Instead, report them on line 7. If the partnership has more than one activity, attach a statement to Schedule K-1 that identifies the activity to which the section 1231 gain (loss) relates.

Attach a statement to each Schedule K-1 indicating the aggregate amount of all section 1231 gains from property held more than 5 years. Do not include any section 1231 gain attributable to straight-line depreciation from section 1250 property. Indicate on the statement that this amount should be included in the partner's computation of qualified 5-year gain only if the amount on the partner's Form 4797, line 7, is more than zero, and that none of the gain is unrecaptured section 1250 gain.

#### Line 7—Other Income (Loss)

Use line 7 to report other items of income, gain, or loss not included on lines 1 through 6. If the partnership has more than one activity, identify on an attachment the amount and the activity to which each amount relates.

If the partnership had a gain from the disposition of non-depreciable personal property used in a trade or business and held it more than 5 years, show the total of all such gains on an attachment to Schedule K-1. Indicate on the statement that the partner should include this amount on line 5 of the worksheet for line 29 of Schedule D (Form 1040). If the partnership has more than one activity, identify on an attachment the amount and the activity to which each amount relates.

Include the following items on line 7:



- Gains from the disposition of farm recapture property (see Form 4797) and other items to which section 1252 applies.
- Gains from the disposition of an interest in oil, gas, geothermal, or other mineral properties (section 1254).
- Any net gain or loss from section 1256 contracts from **Form 6781**, Gains and Losses From Section 1256 Contracts and Straddles.
- Recoveries of tax benefit items (section 111).
- Gambling gains and losses subject to the limitations in section 165(d).
- Any income, gain, or loss to the partnership under section 751(b).
- Specially allocated ordinary gain (loss).
- Net gain (loss) from involuntary conversions due to casualty or theft. The amount for this line is shown on **Form 4684**, Casualties and Thefts, line 38a, 38b, or 39.

Each partner's share must be entered on Schedule K-1. Give each partner a schedule that shows the amounts to be reported on the partner's Form 4684, line 34, columns (b)(i), (b)(ii), and (c).

If there was a gain (loss) from a casualty or theft to property not used in a trade or business or for income-producing purposes, notify the partner. The partnership should not complete Form 4684 for this type of casualty or theft. Instead, each partner will complete his or her own Form 4684.

- Gain from the sale or exchange of qualified small business stock (as defined in the instructions for Schedule D) that is eligible for the 50% section 1202 exclusion. The section 1202 exclusion applies only to qualified small business stock issued after August 10, 1993, and held by the partnership for more than 5 years. Corporate partners are not eligible for the section 1202 exclusion. Additional limitations apply at the partner level. Report each partner's share of section 1202 gain on Schedule K-1. Each partner will determine if he or she qualifies for the section 1202 exclusion. Report on an attachment to Schedule K-1 for each sale or exchange the name of the corporation that issued the stock, the partner's share of the partnership's adjusted basis and sales price of the stock, and the dates the stock was bought and sold.
- Gain eligible for section 1045 rollover (replacement stock purchased by the partnership). Include only gain from the sale or exchange of qualified small business stock (as defined in the instructions for Schedule D) that was deferred by the partnership under section 1045 and reported on Schedule D. See the instructions for Schedule D for more details. Corporate partners are not eligible for the section 1045 rollover. Additional limitations apply at the partner level. Report each partner's share of the gain eligible for section 1045 rollover on Schedule K-1. Each partner will determine if he or she qualifies for the rollover. Report on an attachment to Schedule K-1 for each sale or exchange the name of the corporation that issued

the stock, the partner's share of the partnership's adjusted basis and sales price of the stock, and the dates the stock was bought and sold.

- Gain eligible for section 1045 rollover (replacement stock not purchased by the partnership). Include only gain from the sale or exchange of qualified small business stock (as defined in the instructions for Schedule D) the partnership held for more than 6 months but that **was not** deferred by the partnership under section 1045. See the instructions for Schedule D for more details. A partner (other than a corporation) may be eligible to defer his or her distributive share of this gain under section 1045 if he or she purchases other qualified small business stock during the 60-day period that began on the date the stock was sold by the partnership. Additional limitations apply at the partner level. Report on an attachment to Schedule K-1 for each sale or exchange the name of the corporation that issued the stock, the partner's share of the partnership's adjusted basis and sales price of the stock, and the dates the stock was bought and sold.

## Deductions

### Line 8—Charitable Contributions

Enter the total amount of charitable contributions made by the partnership during its tax year on Schedule K. Enter each partner's distributive share on Schedule K-1. On an attachment to Schedules K and K-1, show separately the dollar amount of contributions subject to each of the 50%, 30%, and 20% of adjusted gross income limits. For additional information, see **Pub. 526**, Charitable Contributions.

Generally, no deduction is allowed for any contribution of \$250 or more unless the partnership obtains a written acknowledgment from the charitable organization that shows the amount of cash contributed, describes any property contributed, and gives an estimate of the value of any goods or services provided in return for the contribution. The acknowledgment must be obtained by the due date (including extensions) of the partnership return or, if earlier, the date the partnership files its return. Do not attach the acknowledgment to the tax return, but keep it with the partnership's records. These rules apply in addition to the filing requirements for Form 8283 described below.

Certain contributions made to an organization conducting lobbying activities are not deductible. See section 170(f)(9) for more details.

**Form 8283**, Noncash Charitable Contributions, must be completed and attached to Form 1065 if the deduction claimed for noncash contributions exceeds \$500. The partnership must give a copy of its Form 8283 to every partner if the deduction for an item or group of similar items of contributed property exceeds \$5,000. Each partner must be

furnished a copy even if the amount allocated to any partner is \$5,000 or less.

If the deduction for an item or group of similar items of contributed property is \$5,000 or less, the partnership should pass through each partner's share of the amount of noncash contributions so the partners will be able to complete their own Forms 8283. See the Instructions for Form 8283 for additional information.

If the partnership made a qualified conservation contribution, include the FMV of the underlying property before and after the donation and describe the conservation purpose furthered by the donation. Give a copy of this information to each partner.

### Line 9—Section 179 Expense Deduction

A partnership may elect to expense part of the cost of certain tangible property the partnership purchased this year for use in its trade or business or certain rental activities. See Pub. 946 for a definition of what kind of property qualifies for the section 179 expense deduction and the Instructions for Form 4562 for limitations on the amount of the section 179 expense deduction.

Complete Part I of Form 4562 to figure the partnership's section 179 expense deduction. The partnership does not claim the deduction itself but instead passes it through to the partners. Attach Form 4562 to Form 1065 and show the total section 179 expense deduction on Schedule K, line 9. Report each partner's allocable share on Schedule K-1, line 9. Do not complete line 9 of Schedule K-1 for any partner that is an estate or trust.

If the partnership is an enterprise zone business, also report on an attachment to Schedules K and K-1 the cost of section 179 property placed in service during the year that is qualified zone property.

See the instructions for line 25 of Schedule K-1, item 4, for any recapture of a section 179 amount.

### Line 10—Deductions Related to Portfolio Income

Enter on line 10 and attach an itemized list of the deductions clearly and directly allocable to portfolio income (other than interest expense and section 212 expenses from a REMIC). Interest expense related to portfolio income is investment interest expense and is reported on line 14a of Schedules K and K-1. Section 212 expenses from the partnership's interest in a REMIC are reported on an attachment for line 4f of Schedules K and K-1.

No deduction is allowable under section 212 for expenses allocable to a convention, seminar, or similar meeting.

### Line 11—Other Deductions

Use line 11 to report deductions not included on lines 8, 9, 10, 17g, and 18b. On an attachment, identify the deduction and amount and, if the partnership has more than one activity, the activity to which the deduction relates.

Examples of items to be reported on an attachment to line 11 include:

- Amounts paid by the partnership that would be allowed as itemized deductions on any of the partners' income tax returns if they were paid directly by a partner for the same purpose. However, do not enter expenses related to portfolio income or investment interest expense on this line.

If there was a loss from an involuntary conversion due to casualty or theft of income-producing property, include in the total amount for this line the relevant amount from Form 4684, line 32.

- Any penalty on early withdrawal of savings.
- Soil and water conservation expenditures (section 175).
- Expenditures for the removal of architectural and transportation barriers to the elderly and handicapped and which the partnership has elected to treat as a current expense (section 190).
- Contributions to a capital construction fund.
- Any amounts paid during the tax year for health insurance coverage for a partner (including that partner's spouse and dependents). For 2002, a partner may be allowed to deduct up to 70% of such amounts on Form 1040, line 30.
- Payments for a partner to an IRA, qualified plan, or simplified employee pension (SEP) or SIMPLE IRA plan. If a qualified plan is a defined benefit plan, a partner's distributive share of payments is determined in the same manner as his or her distributive share of partnership taxable income. For a defined benefit plan, attach to the Schedule K-1 for each partner a statement showing the amount of benefit accrued for the tax year.
- Interest expense allocated to debt-financed distributions. See Notice 89-35 for more information.
- Interest paid or accrued on debt properly allocable to each general partner's share of a working interest in any oil or gas property (if the partner's liability is not limited). General partners that did not materially participate in the oil or gas activity treat this interest as investment interest; for other general partners, it is trade or business interest.

## Credits

### Line 12a—Low-Income Housing Credit

Section 42 provides a credit that may be claimed by owners of low-income residential rental buildings. If the partners are eligible to take the low-income housing credit, complete and attach **Form 8586**, Low-Income Housing Credit; **Form 8609**, Low-Income Housing Credit Allocation Certification; and **Schedule A (Form 8609)**, Annual Statement, to Form 1065.

Report on line 12a(1) the total low-income housing credit for property with respect to which a partnership is to be treated under section 42(j)(5) as the taxpayer to which the low-income housing

credit was allowed. Report any other low-income housing credit on line 12a(2).

If part or all of the credit reported on line 12a(1) or 12a(2) is attributable to additions to qualified basis of property placed in service before 1990, report on an attachment to Schedules K and K-1 the amount of the credit on each line that is attributable to property placed in service **(a)** before 1990 and **(b)** after 1989.

### Line 12b—Qualified Rehabilitation Expenditures Related to Rental Real Estate Activities

Enter total qualified rehabilitation expenditures related to rental real estate activities of the partnership. Also complete the applicable lines of **Form 3468**, Investment Credit, that apply to qualified rehabilitation expenditures for property related to rental real estate activities of the partnership for which income or loss is reported on line 2 of Schedule K. See Form 3468 for details on qualified rehabilitation expenditures. Attach Form 3468 to Form 1065.

For line 12b of Schedule K-1, enter each partner's distributive share of the expenditures. On the dotted line to the left of the entry space for line 12b, enter the line number of Form 3468 on which the partner should report the expenditures. If there is more than one type of expenditure, or the expenditures are from more than one rental real estate activity, report this information separately for each expenditure or activity on an attachment to Schedules K and K-1.



*Qualified rehabilitation expenditures for property not related to rental real estate activities must be listed separately on line 25 of Schedule K-1.*

### Line 12c—Credits (Other Than Credits Shown on Lines 12a and 12b) Related to Rental Real Estate Activities

Report any information that the partners need to figure credits related to a rental real estate activity, other than the low-income housing credit and qualified rehabilitation expenditures. On the dotted line to the left of the entry space for line 12c (or in the margin), identify the type of credit. If there is more than one type of credit or the credit is from more than one activity, report this information separately for each credit or activity on an attachment to Schedules K and K-1.

### Line 12d—Credits Related to Other Rental Activities

Use this line to report information that the partners need to figure credits related to a rental activity other than a rental real estate activity. On the dotted line to the left of the entry space for line 12d, identify the type of credit. If there is more than one type of credit or the credit is from more than one activity, report this information separately for each credit or activity on an attachment to Schedules K and K-1.

## Line 13—Other Credits

Enter on line 13 any other credit, except credits or expenditures shown or listed for lines 12a through 12d of Schedules K and K-1. On the dotted line to the left of the entry space for line 13, identify the type of credit. If there is more than one type of credit or the credit is from more than one activity, report this information separately for each credit or activity on an attachment to Schedules K and K-1. The credits to be reported on line 13 and other required attachments are as follows:

- Credit for backup withholding on dividends, interest, or patronage dividends.
  - Nonconventional source fuel credit. The credit is figured at the partnership level and then is apportioned to the partners based on their distributive shares of partnership income attributable to sales of qualified fuels. Attach a separate schedule to the return to show the computation of the credit. See section 29 for more information.
  - Qualified electric vehicle credit (Form 8834).
  - Unused credits from cooperatives. The unused credits are apportioned to persons who were partners in the partnership on the last day of the partnership's tax year.
  - Work opportunity credit (Form 5884). This credit is apportioned among the partners according to their interest in the partnership at the time the wages on which the credit is figured were paid or accrued.
  - Welfare-to-work credit (Form 8861). This credit is apportioned in the same manner as the work opportunity credit.
  - Credit for alcohol used as fuel (Form 6478). This credit is apportioned to persons who were partners on the last day of the partnership's tax year. The credit must be included in income on page 1, line 7, of Form 1065. See section 40(f) for an election the partnership can make to not have the credit apply.
- If this credit includes the small ethanol producer credit, identify on a statement attached to each Schedule K-1 **(a)** the amount of the small producer credit included in the total credit allocated to the partner, **(b)** the number of gallons of qualified ethanol fuel production allocated to the partner, and **(c)** the partner's share in gallons of the partnership's productive capacity for alcohol.
- Credit for increasing research activities (Form 6765).
  - Enhanced oil recovery credit (Form 8830).
  - Disabled access credit (Form 8826).
  - Renewable electricity production credit (Form 8835).
  - Empowerment zone and renewal community employment credit (Form 8844).
  - Indian employment credit (Form 8845).
  - Credit for employer social security and Medicare taxes paid on certain employee tips (Form 8846).
  - Orphan drug credit (Form 8820).
  - New markets credit (Form 8874).



- Credit for contributions to selected community development corporations (Form 8847).
- Credit for small employer pension start-up costs (Form 8881).
- Credit for employer-provided child care facilities and services (Form 8882).
- New York Liberty Zone business employee credit (Form 8884).
- General credits from an electing large partnership.

See the instructions for line 25, item 13 of Schedule K-1 to report expenditures qualifying for the (a) rehabilitation credit not related to rental real estate activities, (b) energy credit, or (c) reforestation credit.

### Investment Interest

Lines 14a through 14b(2) must be completed for all partners.

#### Line 14a—Interest Expense on Investment Debts

Include on this line interest paid or accrued on debt properly allocable to property held for investment. Property held for investment includes property that produces income (unless derived in the ordinary course of a trade or business) from interest, dividends, annuities, or royalties; and gains from the disposition of property that produces those types of income or is held for investment.

Property held for investment also includes each general partner's share of a working interest in any oil or gas property for which the partner's liability is not limited and in which the partner did not materially participate. However, the level of each partner's participation in an activity is determined by the partner and not by the partnership. As a result, interest allocable to a general partner's share of a working interest in any oil or gas property (if the partner's liability is not

limited) should not be reported on line 14a. Instead, report this interest on line 11.

Investment interest does not include interest expense allocable to a passive activity.

The amount on line 14a will be deducted (after applying the investment interest expense limitations of section 163(d)) by individual partners on Schedule A (Form 1040), line 13.

For more information, see Form 4952.

#### Lines 14b(1) and 14b(2)—Investment Income and Expenses

Enter on line 14b(1) only the investment income included on lines 4a, 4b, 4c, and 4f of Schedules K and K-1. Do not include other portfolio gains or losses on this line.

Enter on line 14b(2) only the investment expense included on line 10 of Schedules K and K-1.

If there are other items of investment income or expense included in the amounts that must be passed through separately to the partner on Schedule K-1 (such as net short-term capital gain or loss, net long-term capital gain or loss, and other portfolio gains or losses) give each partner a schedule identifying these amounts.

Investment income includes gross income from property held for investment, the excess of net gain from the disposition of property held for investment over net capital gain from the disposition of property held for investment, and any net capital gain from the disposition of property held for investment that each partner elects to include in investment income under section 163(d)(4)(B)(iii). Generally, investment income and investment expenses do not include any income or expenses from a passive activity.

Property subject to a net lease is not treated as investment property because it is subject to the passive loss rules. Do not reduce investment income by losses from passive activities.

Investment expenses are deductible expenses (other than interest) directly connected with the production of investment income. See the Form 4952 instructions for more information on investment income and expenses.

### Self-Employment

**Note:** If the partnership is an options dealer or a commodities dealer, see section 1402(i) before completing lines 15a, 15b, and 15c, to determine the amount of any adjustment that may have to be made to the amounts shown on the **Worksheet for Figuring Net Earnings (Loss) From Self-Employment** below. If the partnership is engaged solely in the operation of a group investment program, earnings from the operation are not self-employment earnings for either general or limited partners.

### Worksheet Instructions

**Line 1b.** Include on line 1b any part of the net income (loss) from rental real estate activities from Schedule K, line 2, that is from:

1. Rentals of real estate held for sale to customers in the course of a trade or business as a real estate dealer or
2. Rentals for which services were rendered to the occupants (other than services usually or customarily rendered for the rental of space for occupancy only). The supplying of maid service is such a service; but the furnishing of heat and light, the cleaning of public entrances, exits, stairways and lobbies, trash collection, etc., are not considered services rendered to the occupants.

## Worksheet for Figuring Net Earnings (Loss) From Self-Employment

<b>1a</b> Ordinary income (loss) (Schedule K, line 1) . . . . .	<b>1a</b>		
<b>b</b> Net income (loss) from <b>certain</b> rental real estate activities (see instructions) . . . . .	<b>1b</b>		
<b>c</b> Net income (loss) from other rental activities (Schedule K, line 3c) . . . . .	<b>1c</b>		
<b>d</b> Net loss from Form 4797, Part II, line 18, included on line 1a above. Enter as a positive amount . . . . .	<b>1d</b>		
<b>e</b> Combine lines 1a through 1d . . . . .	<b>1e</b>		
<b>2</b> Net gain from Form 4797, Part II, line 18, included on line 1a above . . . . .	<b>2</b>		
<b>3a</b> Subtract line 2 from line 1e. If line 1e is a loss, increase the loss on line 1e by the amount on line 2 . . . . .	<b>3a</b>		
<b>b</b> Part of line 3a allocated to limited partners, estates, trusts, corporations, exempt organizations, and IRAs . . . . .	<b>3b</b>		
<b>c</b> Subtract line 3b from line 3a. If line 3a is a loss, reduce the loss on line 3a by the amount on line 3b. Include each individual general partner's share on line 15a of Schedule K-1 . . . . .			<b>3c</b>
<b>4a</b> Guaranteed payments to partners (Schedule K, line 5) derived from a trade or business as defined in section 1402(c) (see instructions) . . . . .	<b>4a</b>		
<b>b</b> Part of line 4a allocated to individual limited partners for <b>other than</b> services and to estates, trusts, corporations, exempt organizations, and IRAs . . . . .	<b>4b</b>		
<b>c</b> Subtract line 4b from line 4a. Include each individual general partner's share and each individual limited partner's share on line 15a of Schedule K-1 . . . . .			<b>4c</b>
<b>5</b> Net earnings (loss) from self-employment. Combine lines 3c and 4c. Enter here and on Schedule K, line 15a			<b>5</b>

**Lines 3b and 4b.** Allocate the amounts on these lines in the same way Form 1065, page 1, line 22, is allocated to these particular partners.

**Line 4a.** Include in the amount on line 4a any guaranteed payments to partners reported on Schedules K and K-1, line 5, and derived from a trade or business as defined in section 1402(c). Also include other ordinary income and expense items (other than expense items subject to separate limitations at the partner level, such as the section 179 expense deduction) reported on Schedules K and K-1 that are used to figure self-employment earnings under section 1402.

**General partners.** General partners' net earnings (loss) from self-employment do not include:

- Dividends on any shares of stock and interest on any bonds, debentures, notes, etc., unless the dividends or interest are received in the course of a trade or business, such as a dealer in stocks or securities or interest on notes or accounts receivable.
- Rentals from real estate, except rentals of real estate held for sale to customers in the course of a trade or business as a real estate dealer or payments for rooms or space when significant services are provided.
- Royalty income, except royalty income received in the course of a trade or business.

See the instructions for **Schedule SE (Form 1040)**, Self-Employment Tax, for more information.

**Limited partners.** Generally, a limited partner's share of partnership income (loss) is not included in net earnings (loss) from self-employment. Limited partners treat as self-employment earnings only guaranteed payments for services they actually rendered to, or on behalf of, the partnership to the extent that those payments are payment for those services.

### Line 15a—Net Earnings (Loss) From Self-Employment

**Schedule K.** Enter on line 15a the amount from line 5 of the worksheet.

**Schedule K-1.** Do not complete this line for any partner that is an estate, trust, corporation, exempt organization, or individual retirement arrangement (IRA).

Enter on line 15a of Schedule K-1 each individual general partner's share of the amount shown on line 5 of the worksheet and each individual limited partner's share of the amount shown on line 4c of the worksheet.

### Line 15b—Gross Farming or Fishing Income

Enter the partnership's gross farming or fishing income from self-employment. Individual partners need this amount to figure net earnings from self-employment under the farm optional method in Section B, Part II of Schedule SE (Form 1040).

### Line 15c—Gross Nonfarm Income

Enter the partnership's gross nonfarm income from self-employment. Individual partners need this amount to figure net earnings from self-employment under the nonfarm optional method in Section B, Part II of Schedule SE (Form 1040).

### Adjustments and Tax Preference Items

Lines 16a through 16e must be completed for all partners except certain small corporations exempt from the alternative minimum tax (AMT) under section 55(e).

Enter items of income and deductions that are adjustments or tax preference items for the AMT. See **Form 6251**, Alternative Minimum Tax—Individuals; **Form 4626**, Alternative Minimum Tax—Corporations; or Schedule I of **Form 1041**, U.S. Income Tax Return for Estates and Trusts, to determine the amounts to enter and for other information.

Do not include as a tax preference item any qualified expenditures to which an election under section 59(e) may apply. Instead, report these expenditures on lines 18a and 18b. Because these expenditures are subject to an election by each partner, the partnership cannot figure the amount of any tax preference related to them.

### Line 16a—Depreciation Adjustment on Property Placed in Service After 1986

Figure the adjustment for line 16a based only on tangible property placed in service after 1986 (and tangible property placed in service after July 31, 1986, and before 1987 for which the partnership elected to use the general depreciation system). **Do not** make an adjustment for motion picture films, videotapes, sound recordings, certain public utility property (as defined in section 168(f)(2)), property depreciated under the unit-of-production method (or any other method not expressed in a term of years), or qualified Indian reservation property.

For property placed in service **before 1999**, refigure depreciation for the AMT as follows (using the same convention used for the regular tax):

- For section 1250 property (generally, residential rental and nonresidential real property), use the straight line method over 40 years.
- For tangible property (other than section 1250 property) depreciated using the straight line method for the regular tax, use the straight line method over the property's class life. Use 12 years if the property has no class life.
- For any other tangible property, use the 150% declining balance method, switching to the straight line method the first year it gives a larger deduction, over the property's AMT class life. Use 12 years if the property has no class life.

**Note:** See *Pub. 946* for a table of class lives.

For property placed in service **after 1998**, refigure depreciation for the AMT **only** for property depreciated for the regular tax using the 200% declining balance method. For the AMT, use the 150% declining balance method, switching to the straight line method the first tax year it gives a larger deduction, and the same convention and recovery period used for the regular tax.

Figure the adjustment by subtracting the AMT deduction for depreciation from the regular tax deduction and enter the result on line 14a. If the AMT deduction is more than the regular tax deduction, enter the difference as a negative amount. Depreciation capitalized to inventory must also be refigured using the AMT rules. Include on this line the current year adjustment to income, if any, resulting from the difference.

### Line 16b—Adjusted Gain or Loss

If the partnership disposed of any tangible property placed in service after 1986 (or after July 31, 1986, if an election was made to use the general depreciation system), or if it disposed of a certified pollution control facility placed in service after 1986, refigure the gain or loss from the disposition using the adjusted basis for the AMT. The property's adjusted basis for the AMT is its cost or other basis minus all depreciation or amortization deductions allowed or allowable for the AMT during the current tax year and previous tax years. Enter on this line the difference between the regular tax gain (or loss) and the AMT gain (or loss). If the AMT gain is less than the regular tax gain, **or** the AMT loss is more than the regular tax loss, **or** there is an AMT loss and a regular tax gain, enter the difference as a negative amount.

If any part of the adjustment is allocable to net short-term capital gain (loss), net long-term capital gain (loss), or net section 1231 gain (loss), attach a schedule that identifies the amount of the adjustment allocable to each type of gain or loss. For a net long-term capital gain (loss), also identify the amount of the adjustment that is 28% rate gain (loss). For a net section 1231 gain (loss), also identify the amount of adjustment that is unrecaptured section 1250 gain.

No schedule is required if the adjustment is allocable solely to ordinary gain (loss).

### Line 16c—Depletion (Other Than Oil and Gas)

Do not include any depletion on oil and gas wells. The partners must figure their depletion deductions and preference items separately.

Refigure the depletion deduction under section 611 for mines, wells (other than oil and gas wells), and other natural deposits for the AMT. Percentage depletion is limited to 50% of the taxable income from the property as figured under section 613(a), using only income and deductions allowed for the AMT. Also, the deduction is limited to the property's



adjusted basis at the end of the year, as refigured for the AMT. Figure this limit separately for each property. When refiguring the property's adjusted basis, take into account any AMT adjustments made this year or in previous years that affect basis (other than the current year's depletion).

Enter the difference between the regular tax and AMT deduction. If the AMT deduction is greater, enter the difference as a negative amount.

### Lines 16d(1) and 16d(2)

Enter only the income and deductions for oil, gas, and geothermal properties that are used to figure the partnership's ordinary income or loss (line 22 of Form 1065). If there are items of income or deduction for oil, gas, and geothermal properties included in the amounts required to be passed through separately to the partners on Schedule K-1 (items not reported on line 1 of Schedule K-1), give each partner a schedule identifying these amounts.

Figure the amount for lines 16d(1) and (2) separately for oil and gas properties that are not geothermal deposits and for all properties that are geothermal deposits.

Give each partner a schedule that shows the separate amounts that are included in the computation of the amounts on lines 16d(1) and (2).

**Line 16d(1)—Gross income from oil, gas, and geothermal properties.** Enter the aggregate amount of gross income (within the meaning of section 613(a)) from all oil, gas, and geothermal properties that was received or accrued during the tax year and included on page 1, Form 1065.

**Line 16d(2)—Deductions allocable to oil, gas, and geothermal properties.** Enter the amount of any deductions allowed for the AMT that are allocable to oil, gas, and geothermal properties.

### Line 16e—Other Adjustments and Tax Preference Items

Attach a schedule that shows each partner's share of other items not shown on lines 16a through 16d(2) that are adjustments or tax preference items or that the partner needs to complete Form 6251, Form 4626, or Schedule I of Form 1041. See these forms and their instructions to determine the amount to enter.

Other adjustments and tax preference items or information the partner needs include the following:

- Accelerated depreciation of real property under pre-1987 rules.
- Accelerated depreciation of leased personal property under pre-1987 rules.
- Long-term contracts entered into after February 28, 1986. Except for certain home construction contracts, the taxable income from these contracts must be figured using the percentage of completion method of accounting for the AMT.

- Losses from tax shelter farm activities. No loss from any tax shelter farm activity is allowed for the AMT.

- Any information needed by certain corporate partners to compute the adjusted current earnings (ACE) adjustment.

### Foreign Taxes

Lines 17a through 17h must be completed if the partnership has foreign income, deductions, or losses or has paid or accrued foreign taxes. See **Pub. 514**, Foreign Tax Credit for Individuals, for more information.

### Line 17a—Name of Foreign Country or U.S. Possession

Enter the name of the foreign country or U.S. possession from which the partnership had income or to which the partnership paid or accrued taxes. If the partnership had income from, or paid or accrued taxes to, **more than one** foreign country or U.S. possession, enter "**See attached**" and attach a schedule for each country for lines 17a through 17h.

### Line 17b—Gross Income From All Sources

Enter the partnership's gross income from all sources (both U.S. and foreign source).

### Line 17c—Gross Income Sourced at Partner Level

Enter the total gross income of the partnership that is required to be sourced at the partner level. This includes income from the sale of most personal property other than inventory, depreciable property, and certain intangible property. See Pub. 514 and section 865 for details. Attach a schedule showing the following information:

- The amount of this gross income (without regard to its source) in each category identified in the instructions for line 17d, including each of the listed categories.
- Specifically identify gains on the sale of personal property other than inventory, depreciable property, and certain intangible property on which a foreign tax of 10% or more was paid or accrued. Also list losses on the sale of such property if the foreign country would have imposed a 10% or higher tax had the sale resulted in a gain. See **Sales or Exchanges of Certain Personal Property** in Pub. 514 and section 865.
- Specify the net foreign source capital gain or loss within each separate limitation category shown below in the instructions for Line 17d(2). Also, in the case of noncorporate partners, separately identify the net foreign source gain or loss within each separate limitation category that is 28% rate gain or loss, unrecaptured section 1250 gain, and qualified 5-year gain.

### Line 17d—Foreign Gross Income Sourced at Partnership Level

Separately report gross income from sources outside the United States by category of income as follows. For

partnership and corporate partners only, attach a schedule identifying the total amount of foreign gross income in each category of income attributable to foreign branches. See Pub. 514 for information on the categories of income.

**Line 17d(1).** Passive foreign source income.

**Line 17d(2).** Attach a schedule showing the amount of foreign source income included in each of the following listed categories of income:

- Financial services income;
- High withholding tax interest;
- Shipping income;
- Dividends from each noncontrolled section 902 corporation;
- Dividends from a domestic international sales corporation (DISC) or a former DISC;
- Distributions from a foreign sales corporation (FSC) or a former FSC;
- Section 901(j) income; and
- Certain income re-sourced by treaty.

**Line 17d(3).** General limitation foreign source income (all other foreign source income).

### Line 17e—Deductions Allocated and Apportioned at Partner Level

Enter on line 17e(1) the partnership's total interest expense (including interest equivalents under Temporary Regulations section 1.861-9T(b)). Do not include interest directly allocable under Temporary Regulations section 1.861-10T to income from a specific property. This type of interest is allocated and apportioned at the partnership level and is included on lines 17f(1) through (3). On line 17e(2), enter the total of all other deductions or losses that are required to be allocated at the partner level. For example, include on line 17e(2) research and experimental expenditures (see Regulations section 1.861-17(f)).

### Line 17f—Deductions Allocated and Apportioned at Partnership Level to Foreign Source Income

Separately report partnership deductions that are apportioned at the partnership level to (1) passive foreign source income, (2) each of the listed foreign categories of income, and (3) general limitation foreign source income (see the instructions for line 17d). See Pub. 514 for more information.

For partnership and corporate partners only, attach a schedule identifying the total amount of deductions apportioned to each category of income shown in the instructions for line 17d that are attributable to foreign branches.

### Line 17g—Total Foreign Taxes

Enter in U.S. dollars the total foreign taxes (described in section 901 or section 903) that were paid or accrued by the partnership (according to its method of accounting for such taxes). Translate these amounts into U.S. dollars by using the applicable exchange rate (see Pub. 514).

Attach a schedule reporting the following information:

1. The total amount of foreign taxes (including foreign taxes on income sourced at the partner level) relating to each category of income (see instructions for line 17d).

2. The dates on which the taxes were paid or accrued, the exchange rates used, and the amounts in both foreign currency and U.S. dollars, for:

- Taxes withheld at source on interest.
- Taxes withheld at source on dividends.
- Taxes withheld at source on rents and royalties.
- Other foreign taxes paid or accrued.

### Line 17h—Reduction in Taxes Available for Credit

Enter the total reductions in taxes available for credit.

Attach a schedule showing the reductions for:

- Taxes on foreign mineral income (section 901(e)).
- Taxes on foreign oil and gas extraction income (section 907(a)).
- Taxes attributable to boycott operations (section 908).
- Failure to timely file (or furnish all of the information required on) Forms 5471 and 8865.
- Any other items (specify).

### Other

### Lines 18a and 18b

Generally, section 59(e) allows each partner to make an election to deduct the partner's distributive share of the partnership's otherwise deductible qualified expenditures ratably over 10 years (3 years for circulation expenditures), beginning with the tax year in which the expenditures were made (or for intangible drilling and development costs, over the 60-month period beginning with the month in which such costs were paid or incurred). The term "qualified expenditures" includes only the following types of expenditures paid or incurred during the tax year:

- Circulation expenditures.
- Research and experimental expenditures.
- Intangible drilling and development costs.
- Mining exploration and development costs.

If a partner makes this election, these items are not treated as tax preference items.

Because the partners are generally allowed to make this election, the partnership cannot deduct these amounts or include them as adjustments or tax preference items on Schedule K-1. Instead, on lines 18a and 18b of Schedule K-1, the partnership passes through the information the partners need to figure their separate deductions.

On line 18a, enter the type of expenditures claimed on line 18b. Enter

on line 18b the qualified expenditures paid or incurred during the tax year to which an election under section 59(e) may apply. Enter this amount for all partners whether or not any partner makes an election under section 59(e). If the expenditures are for intangible drilling and development costs, enter the month in which the expenditures were paid or incurred (after the type of expenditure on line 18a). If there is more than one type of expenditure included in the total shown on line 18b (or intangible drilling and development costs were paid or incurred for more than 1 month), report this information separately for each type of expenditure (or month) on an attachment to Schedules K and K-1.

### Line 19—Tax-Exempt Interest Income

Enter on line 19 tax-exempt interest income, including any exempt-interest dividends received from a mutual fund or other regulated investment company. Individual partners must report this information on line 8b of Form 1040. The adjusted basis of the partner's interest is increased by the amount shown on this line under section 705(a)(1)(B).

### Line 20—Other Tax-Exempt Income

Enter on line 20 all income of the partnership exempt from tax other than tax-exempt interest (for example, life insurance proceeds). The adjusted basis of the partner's interest is increased by the amount shown on this line under section 705(a)(1)(B).

### Line 21—Nondeductible Expenses

Enter on line 21 nondeductible expenses paid or incurred by the partnership. Do not include separately stated deductions shown elsewhere on Schedules K and K-1, capital expenditures, or items the deduction for which is deferred to a later tax year. The adjusted basis of the partner's interest is decreased by the amount shown on this line under section 705(a)(2)(B).

### Line 22—Distributions of Money (Cash and Marketable Securities)

Enter on line 22 the total distributions to each partner of cash and marketable securities that are treated as money under section 731(c)(1). Generally, marketable securities are valued at FMV on the date of distribution. However, the value of marketable securities does not include the distributee partner's share of the gain on the securities distributed to that partner. See section 731(c)(3)(B) for details.

If the amount on line 22 includes marketable securities treated as money, state separately on an attachment to Schedules K and K-1 (a) the partnership's adjusted basis of those securities immediately before the distribution and (b) the FMV of those securities on the date of distribution (excluding the distributee partner's share of the gain on the securities distributed to that partner).

### Line 23—Distributions of Property Other Than Money

Enter on line 23 the total distributions to each partner of property not included on line 22. In computing the amount of the distribution, use the adjusted basis of the property to the partnership immediately before the distribution. In addition, attach a statement showing the adjusted basis and FMV of each property distributed.

### Line 24 (Schedule K Only)

Attach a statement to report the partnership's total income, expenditures, or other information for the items listed under **Line 25 (Schedule K-1 Only)—Supplemental Information** below.

### Lines 24a and 24b (Schedule K-1 Only)—Recapture of Low-Income Housing Credit

If recapture of part or all of the low-income housing credit is required because (a) prior year qualified basis of a building decreased or (b) the partnership disposed of a building or part of its interest in a building, see **Form 8611, Recapture of Low-Income Housing Credit**. The instructions for Form 8611 indicate when the form is completed by the partnership and what information is provided to partners when recapture is required.

If a partner's ownership interest in a building decreased because of a transaction at the partner level, the partnership must provide the necessary information to the partner to enable the partner to figure the recapture.

Report on line 24a the total low-income housing credit recapture with respect to a partnership treated under section 42(j)(5) as the taxpayer to which the low-income housing credit was allowed. Report any other low-income housing credit recapture on line 24b.

If the partnership filed **Form 8693, Low-Income Housing Credit Disposition Bond**, to avoid recapture of the low-income housing credit, no entry should be made on line 24 of Schedule K-1.

See Form 8586, Form 8611, and section 42 for more information.

### Line 25 (Schedule K-1 Only)—Supplemental Information

Enter in the line 25 Supplemental Information space of Schedule K-1, or on an attached schedule if more space is needed, each partner's share of any information requested on lines 1 through 24b that must be reported in detail, and the following items 1 through 27. Identify the applicable line number next to the information entered in the Supplemental Information space. Show income or gains as a positive number. Show losses in parentheses.

1. Taxes paid on undistributed capital gains by a regulated investment company or a real estate investment trust (REIT). As a shareholder of a regulated investment company or a REIT, the partnership will receive notice on **Form**



**2439**, Notice to Shareholder of Undistributed Long-Term Capital Gains, of the amount of tax paid on undistributed capital gains.

**2.** The number of gallons of each fuel sold or used during the tax year for a nontaxable use qualifying for the credit for taxes paid on fuels, type of use, and the applicable credit per gallon. See **Form 4136**, Credit for Federal Tax Paid on Fuels, for details.

**3.** The partner's share of gross income from each property, share of production for the tax year, etc., needed to figure the partner's depletion deduction for oil and gas wells. The partnership should also allocate to each partner a proportionate share of the adjusted basis of each partnership oil or gas property. The allocation of the basis of each property is made as specified in section 613A(c)(7)(D).

The partnership cannot deduct depletion on oil and gas wells. The partner must determine the allowable amount to report on his or her return. See Pub. 535 for more information.

**4.** Recapture of section 179 expense deduction. For property placed in service after 1986, the section 179 expense deduction is recaptured at any time the business use of the property drops to 50% or less. Enter the amount that was originally passed through to the partners and the partnership's tax year in which the amount was passed through. Inform the partner if the recapture amount was caused by the disposition of the section 179 property. Do not include this amount in the partnership's income.

**5.** Recapture of certain mining exploration expenditures (section 617).

**6.** Any information or statements a partner needs to comply with section 6111 (registration of tax shelters) or section 6662(d)(2)(B)(ii) (regarding adequate disclosure of items that may cause an understatement of income tax).

**7.** The partner's share of preproductive period farm expenses, if the partnership is not required to use the accrual method of accounting. See Regulations section 1.263A-4.

**8.** Any information a partner needs to figure the interest due under section 453(l)(3). If the partnership elected to report the disposition of certain timeshares and residential lots on the installment method, each partner's tax liability must be increased by the partner's allocable share of the interest on tax attributable to the installment payments received during the tax year.

**9.** Any information a partner needs to figure interest due under section 453A(c). If an obligation arising from the disposition of property to which section 453A applies is outstanding at the close of the year, report each partner's allocable share of the outstanding installment obligation to which section 453A(b) applies.

**10.** For closely held partnerships (as defined in section 460(b)(4)), provide the information a partner needs to figure the

partner's allocable share of any interest due or to be refunded under the look-back method of section 460(b)(2) on certain long-term contracts that are accounted for under either the percentage of completion-capitalized cost method or the percentage of completion method. Also attach to Form 1065 the information specified in the Instructions for Form 8697, Part II, lines 1 and 3, for each tax year in which such a long-term contract is completed.

**11.** Any information a partner needs relating to interest expense that the partner is required to capitalize. A partner may be required to capitalize interest that was incurred by the partner for the partnership's production expenditures. Similarly, a partner may have to capitalize interest that was incurred by the partnership for the partner's own production expenditures. See Regulations sections 1.263A-8 through 1.263A-15 for more information.

**12.** Any information a partner that is a tax-exempt organization may need to figure its share of unrelated business taxable income under section 512(a)(1) (but excluding any modifications required by paragraphs (8) through (15) of section 512(b)). Partners are required to notify the partnership of their tax-exempt status. See **Form 990-T**, Exempt Organization Business Income Tax Return, for more information.

**13.** Expenditures qualifying for the (a) rehabilitation credit not related to rental real estate activities, (b) energy credit, or (c) reforestation credit. Complete and attach Form 3468. See Form 3468 and the related instructions for information on eligible property and the lines on Form 3468 to complete. Do not include that part of the cost of the property the partnership has elected to expense under section 179. Attach to each Schedule K-1 a separate schedule in a format similar to that shown on Form 3468 detailing each partner's share of qualified expenditures. Also indicate the lines of Form 3468 on which the partners should report these amounts.

**14.** Recapture of investment credit. Complete and attach **Form 4255**, Recapture of Investment Credit, when investment credit property is disposed of, or it no longer qualifies for the credit, before the end of the recapture period or the useful life applicable to the property. State the type of property at the top of Form 4255 and complete lines 2, 4, and 5, whether or not any partner is subject to recapture of the credit. Attach to each Schedule K-1 a separate schedule providing the information the partnership is required to show on Form 4255, but list only the partner's distributive share of the cost of the property subject to recapture. Also indicate the lines of Form 4255 on which the partners should report these amounts.

**15.** Any information a partner may need to figure the recapture of the qualified electric vehicle credit. See Pub. 535 for more information.

**16.** Recapture of new markets credit (see Form 8874).

**17.** Any information a partner may need to figure recapture of the Indian employment credit. Generally, if a partnership terminates a qualified employee less than 1 year after the date of initial employment, any Indian employment credit allowed for a prior tax year by reason of wages paid or incurred to that employee must be recaptured. For details, see section 45A(d).

**18.** Nonqualified withdrawals by the partnership from a capital construction fund.

**19.** Unrecaptured section 1250 gain. Figure this amount for each section 1250 property in Part III of Form 4797 (except property for which gain is reported using the installment method on Form 6252) for which you had an entry in Part I of Form 4797 by subtracting line 26g of Form 4797 from the **smaller** of line 22 or line 24 of Form 4797. Figure the total of these amounts for all section 1250 properties. Generally, the result is the partnership's unrecaptured section 1250 gain. However, if the partnership is reporting gain on the installment method for a section 1250 property held more than 1 year, see the next paragraph to figure the unrecaptured section 1250 gain on that property. Report each partner's distributive share of the total amount as "Unrecaptured section 1250 gain."

The total unrecaptured section 1250 gain for an installment sale of section 1250 property held more than 1 year is figured for the year of the sale in a manner similar to that used in the preceding paragraph. However, the total unrecaptured section 1250 gain must be allocated to the installment payments received from the sale. To do so, the partnership generally must treat the gain allocable to each installment payment as unrecaptured section 1250 gain until all such gain has been used in full. Figure the unrecaptured section 1250 gain for installment payments received during the tax year as the **smaller** of (a) the amount from line 26 or line 37 of Form 6252 (whichever applies) or (b) the total unrecaptured section 1250 gain for the sale reduced by all gain reported in prior years (excluding section 1250 ordinary income recapture). However, if the partnership chose not to treat all of the gain from payments received after May 6, 1997, and before August 24, 1999, as unrecaptured section 1250 gain, use only the amount the partnership chose to treat as unrecaptured section 1250 gain for those payments to reduce the total unrecaptured section 1250 gain remaining to be reported for the sale.

If the partnership received a Schedule K-1 or Form 1099-DIV from an estate, a trust, a REIT, or a mutual fund (or other regulated investment company) reporting "unrecaptured section 1250 gain," **do not** add it to the partnership's own unrecaptured section 1250 gain. Instead, report it as a separate amount. For example, if the partnership received a

Form 1099-DIV from a REIT with unrecaptured section 1250 gain, report it as "Unrecaptured section 1250 gain from a REIT."

Also report as a separate amount any gain from the sale or exchange of an interest in another partnership attributable to unrecaptured section 1250 gain. See Regulations section 1.1(h)-1 and attach the statement required under Regulations section 1.1(h)-1(e).

**20.** If the partnership is a closely held partnership (as defined in section 460(b)(4)) and it depreciated certain property placed in service after September 13, 1995, under the income forecast method, it must attach to Form 1065 the information specified in the instructions for Form 8866, line 2, for the 3rd and 10th tax years beginning after the tax year the property was placed in service. It must also report the line 2 amounts to its partners. See the instructions for Form 8866 for more details.

**21.** Any information a partner that is a publicly traded partnership may need to determine if it meets the 90% qualifying income test of section 7704(c)(2). Partners are required to notify the partnership of their status as a publicly traded partnership.

**22.** Amortization of reforestation expenditures. Report the amortizable basis and year in which the amortization began for the current year and the 7 preceding years. For limits that may apply, see section 194 and Pub. 535.

**23.** Any information needed by a partner to figure the interest due under section 1260(b). If any portion of a constructive ownership transaction was open in any prior year, each partner's tax liability must be increased by the partner's pro rata share of interest due on any deferral of gain recognition. See section 1260(b) for details, including how to figure the interest.

**24.** Extraterritorial income exclusion. See the instructions on page 13 for information that is required to be reported on line 25.

**25.** Commercial revitalization deduction from rental real estate activities. If the deduction is for a nonrental building, it is deducted by the partnership on line 20 of Form 1065. See the instructions for line 20 on page 18 for details.

**26.** If the partnership participates in a reportable tax shelter transaction, attach a copy of the partnership's tax shelter disclosure statement to Schedule K-1 or provide the information each partner will need to complete a tax shelter disclosure statement for the transaction. See **Tax Shelter Disclosure Statement** on page 8 for more information.

If the partnership enters into a transaction defined in section 988(c)(1) (relating to foreign currency transactions) after December 31, 2002, and any partner

that is an individual or trust and has a distributive share of the loss of at least \$50,000, provide those partners with the information they will need to complete Form 8886. Unless the partnership's loss from this transaction is at least \$5 million in a single tax year or \$10 million in any combination of tax years, the partnership is not required to file Form 8886.

**27.** Any other information a partner may need to file his or her return that is not shown anywhere else on Schedule K-1. For example, if one of the partners is a pension plan, that partner may need special information to properly file its tax return.

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## Analysis of Net Income (Loss)

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For each type of partner shown, enter the portion of the amount shown on line 1 that was allocated to that type of partner. Report all amounts for LLC members on the line for limited partners. The sum of the amounts shown on line 2 must equal the amount shown on line 1. In addition, the amount on line 1 must equal the amount on line 9, Schedule M-1 (if the partnership is required to complete Schedule M-1).

In classifying partners who are individuals as "active" or "passive," the partnership should apply the rules below. In applying these rules, a partnership should classify each partner to the best of its knowledge and belief. It is assumed that in most cases the level of a particular partner's participation in an activity will be apparent.

**1.** If the partnership's principal activity is a trade or business, classify a general partner as "active" if the partner materially participated in all partnership trade or business activities; otherwise, classify a general partner as "passive."

**2.** If the partnership's principal activity consists of a working interest in an oil or gas well, classify a general partner as "active."

**3.** If the partnership's principal activity is a rental real estate activity, classify a general partner as "active" if the partner actively participated in all of the partnership's rental real estate activities; otherwise, classify a general partner as "passive."

**4.** Classify as "passive" all partners in a partnership whose principal activity is a rental activity other than a rental real estate activity.

**5.** If the partnership's principal activity is a portfolio activity, classify all partners as "active."

**6.** Classify as "passive" all limited partners and LLC members in a partnership whose principal activity is a trade or business or rental activity.

**7.** If the partnership cannot make a reasonable determination whether a partner's participation in a trade or business activity is material or whether a partner's participation in a rental real estate activity is active, classify the partner as "passive."

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## Schedule L—Balance Sheets per Books

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**Note:** Schedules L, M-1, and M-2 are not required to be completed if the partnership answered **Yes** to Question 5 of Schedule B.

The balance sheets should agree with the partnership's books and records. Attach a statement explaining any differences.

Partnerships reporting to the Interstate Commerce Commission (ICC) or to any national, state, municipal, or other public officer may send copies of their balance sheets prescribed by the ICC or national, state, or municipal authorities, as of the beginning and end of the tax year, instead of completing Schedule L. However, statements filed under this procedure must contain sufficient information to enable the IRS to reconstruct a balance sheet similar to that contained on Form 1065 without contacting the partnership during processing.

All amounts on the balance sheet should be reported in U.S. dollars. If the partnership's books and records are kept in a foreign currency, the balance sheet should be translated in accordance with U.S. generally accepted accounting principles (GAAP).

**Exception.** If the partnership or any qualified business unit of the partnership uses the U.S. dollar approximate separate transactions method, Schedule L should reflect the tax balance sheet prepared and translated into U.S. dollars according to Regulations section 1.985-3(d), and not a U.S. GAAP balance sheet.

## Line 5—Tax-Exempt Securities

Include on this line:

**1.** State and local government obligations, the interest on which is excludable from gross income under section 103(a) and

**2.** Stock in a mutual fund or other regulated investment company that distributed exempt-interest dividends during the tax year of the partnership.

## Line 18—All Nonrecourse Loans

Nonrecourse loans are those liabilities of the partnership for which no partner bears the economic risk of loss.



## Schedule M-1— Reconciliation of Income (Loss) per Books With Income (Loss) per Return

### Line 3—Guaranteed Payments

Include on this line guaranteed payments shown on Schedule K, line 5 (other than amounts paid for insurance that constitutes medical care for a partner, a partner's spouse, and a partner's dependents).

### Line 4b—Travel and Entertainment

Include on this line:

- Meal and entertainment expenses not deductible under section 274(n).
- Expenses for the use of an entertainment facility.
- The part of business gifts over \$25.
- Expenses of an individual allocable to conventions on cruise ships over \$2,000.
- Employee achievement awards over \$400.
- The part of the cost of entertainment tickets that exceeds face value (also subject to 50% limit).
- The part of the cost of skyboxes that exceeds the face value of nonluxury box seat tickets.
- The part of the cost of luxury water travel expenses not deductible under section 274(m).
- Expenses for travel as a form of education.
- Nondeductible club dues.
- Other nondeductible travel and entertainment expenses.

## Schedule M-2—Analysis of Partners' Capital Accounts

Show what caused the changes during the tax year in the partners' capital accounts as reflected on the partnership's books and records. The amounts on Schedule M-2 should equal the total of the amounts reported in Item J of all the partners' Schedules K-1.

The partnership may, but is not required to, use the rules in Regulations section 1.704-1(b)(2)(iv) to determine the partners' capital accounts in Schedule M-2 and Item J of the partners' Schedules K-1. If the beginning and ending capital accounts reported under these rules differ from the amounts reported on Schedule L, attach a statement reconciling any differences.

### Line 2—Capital Contributed During Year

Include on line 2a the amount of money contributed and on line 2b the amount of property contributed by each partner to the partnership as reflected on the partnership's books and records.

### Line 3—Net Income (Loss) per Books

Enter on line 3 the net income (loss) shown on the partnership books from Schedule M-1, line 1.

### Line 6—Distributions

**Line 6a—Cash.** Enter on line 6a the amount of money distributed to each partner by the partnership.

**Line 6b—Property.** Enter the amount of property distributed to each partner by the partnership as reflected on the partnership's books and records. Include withdrawals from inventory for the personal use of a partner.

**Paperwork Reduction Act Notice.** We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form and related schedules will vary depending on individual circumstances. The estimated average times are:

Form	Recordkeeping	Learning about the law or the form	Preparing the form	Copying, assembling, and sending the form to the IRS
1065	41 hr., 59 min.	24 hr., 21 min.	43 hr., 1 min.	4 hr., 49 min.
Schedule D (Form 1065)	6 hr., 56 min.	2 hr., 10 min.	2 hr., 23 min.	
Schedule K-1 (Form 1065)	27 hr., 1 min.	10 hr., 25 min.	11 hr., 19 min.	
Schedule L (Form 1065)	15 hr., 32 min.	6 min.	21 min.	
Schedule M-1 (Form 1065)	3 hr., 21 min.	12 min.	15 min.	
Schedule M-2 (Form 1065)	3 hr., 6 min.	6 min.	9 min.	

If you have comments concerning the accuracy of these time estimates or suggestions for making these forms simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **Do not** send the tax form to this address. Instead, see **Where To File** on page 4.

## Codes for Principal Business Activity and Principal Product or Service

This list of Principal Business Activities and their associated codes is designed to classify an enterprise by the type of activity in which it is engaged to facilitate the administration of the Internal Revenue Code. These Principal Business Activity Codes are based on the North American Industry Classification System.

Using the list of activities and codes below, determine from which activity the business derives the largest percentage of its "total receipts." Total receipts is defined as the sum of gross receipts or sales (page 1, line 1a); all other income (page 1, lines 4 through 7); income reported on Schedule K, lines 3a, 4a, 4b and 4c; income or net gain reported on Schedule K, lines 4d, 4e(1), 4f, 6, and 7; and income or net gain reported on Form 8825, lines 2, 19, and 20a. If the business purchases raw materials and supplies them to a subcontractor to produce the finished product, but retains title to the product, the business is considered a manufacturer and must use one of the manufacturing codes (311110-339900).

Once the Principal Business Activity is determined, enter the six-digit code from the list below on page 1, item C. Also enter a brief description of the business activity in item A and the principal product or service of the business in item B.

### Agriculture, Forestry, Fishing and Hunting

#### Code

#### Crop Production

- 111100 Oilseed & Grain Farming
- 111210 Vegetable & Melon Farming (including potatoes & yams)
- 111300 Fruit & Tree Nut Farming
- 111400 Greenhouse, Nursery, & Floriculture Production
- 111900 Other Crop Farming (including tobacco, cotton, sugarcane, hay, peanut, sugar beet & all other crop farming)

#### Animal Production

- 112111 Beef Cattle Ranching & Farming
- 112112 Cattle Feedlots
- 112120 Dairy Cattle & Milk Production
- 112210 Hog & Pig Farming
- 112300 Poultry & Egg Production
- 112400 Sheep & Goat Farming
- 112510 Animal Aquaculture (including shellfish & finfish farms & hatcheries)
- 112900 Other Animal Production

#### Forestry and Logging

- 113110 Timber Tract Operations
- 113210 Forest Nurseries & Gathering of Forest Products
- 113310 Logging

#### Fishing, Hunting and Trapping

- 114110 Fishing
- 114210 Hunting & Trapping

#### Support Activities for Agriculture and Forestry

- 115110 Support Activities for Crop Production (including cotton ginning, soil preparation, planting, & cultivating)
- 115210 Support Activities for Animal Production
- 115310 Support Activities For Forestry

### Mining

- 211110 Oil & Gas Extraction
- 212110 Coal Mining
- 212200 Metal Ore Mining
- 212310 Stone Mining & Quarrying
- 212320 Sand, Gravel, Clay, & Ceramic & Refractory Minerals Mining & Quarrying
- 212390 Other Nonmetallic Mineral Mining & Quarrying
- 213110 Support Activities for Mining

### Utilities

#### Code

- 221100 Electric Power Generation, Transmission & Distribution
- 221210 Natural Gas Distribution
- 221300 Water, Sewage & Other Systems

### Construction

#### Construction of Buildings

- 236110 Residential Building Construction
- 236200 Nonresidential Building Construction

#### Heavy and Civil Engineering Construction

- 237100 Utility System Construction
- 237210 Land Subdivision
- 237310 Highway, Street, & Bridge Construction
- 237990 Other Heavy & Civil Engineering Construction

#### Specialty Trade Contractors

- 238100 Foundation, Structure, & Building Exterior Contractors (including framing carpentry, masonry, glass, roofing, & siding)
- 238210 Electrical Contractors
- 238220 Plumbing, Heating, & Air-Conditioning Contractors
- 238290 Other Building Equipment Contractors
- 238300 Building Finishing Contractors (including drywall, insulation, painting, wallcovering, flooring, tile, & finish carpentry)
- 238900 Other Specialty Trade Contractors (including site preparation)

### Manufacturing

#### Food Manufacturing

- 311110 Animal Food Mfg
- 311200 Grain & Oilseed Milling
- 311300 Sugar & Confectionery Product Mfg
- 311400 Fruit & Vegetable Preserving & Specialty Food Mfg
- 311500 Dairy Product Mfg
- 311610 Animal Slaughtering and Processing
- 311710 Seafood Product Preparation & Packaging
- 311800 Bakeries & Tortilla Mfg
- 311900 Other Food Mfg (including coffee, tea, flavorings & seasonings)

### Code

#### Beverage and Tobacco Product Manufacturing

- 312110 Soft Drink & Ice Mfg
- 312120 Breweries
- 312130 Wineries
- 312140 Distilleries
- 312200 Tobacco Manufacturing

#### Textile Mills and Textile Product Mills

- 313000 Textile Mills
- 314000 Textile Product Mills

#### Apparel Manufacturing

- 315100 Apparel Knitting Mills
- 315210 Cut & Sew Apparel Contractors
- 315220 Men's & Boys' Cut & Sew Apparel Mfg
- 315230 Women's & Girls' Cut & Sew Apparel Mfg
- 315290 Other Cut & Sew Apparel Mfg
- 315990 Apparel Accessories & Other Apparel Mfg

#### Leather and Allied Product Manufacturing

- 316110 Leather & Hide Tanning & Finishing
- 316210 Footwear Mfg (including rubber & plastics)
- 316990 Other Leather & Allied Product Mfg

#### Wood Product Manufacturing

- 321110 Sawmills & Wood Preservation
- 321210 Veneer, Plywood, & Engineered Wood Product Mfg
- 321900 Other Wood Product Mfg

#### Paper Manufacturing

- 322100 Pulp, Paper, & Paperboard Mills
- 322200 Converted Paper Product Mfg

#### Printing and Related Support Activities

- 323100 Printing & Related Support Activities

#### Petroleum and Coal Products Manufacturing

- 324110 Petroleum Refineries (including integrated)
- 324120 Asphalt Paving, Roofing, & Saturated Materials Mfg
- 324190 Other Petroleum & Coal Products Mfg

#### Chemical Manufacturing

- 325100 Basic Chemical Mfg
- 325200 Resin, Synthetic Rubber, & Artificial & Synthetic Fibers & Filaments Mfg
- 325300 Pesticide, Fertilizer, & Other Agricultural Chemical Mfg
- 325410 Pharmaceutical & Medicine Mfg
- 325500 Paint, Coating, & Adhesive Mfg
- 325600 Soap, Cleaning Compound, & Toilet Preparation Mfg
- 325900 Other Chemical Product & Preparation Mfg

#### Plastics and Rubber Products Manufacturing

- 326100 Plastics Product Mfg
- 326200 Rubber Product Mfg

#### Nonmetallic Mineral Product Manufacturing

- 327100 Clay Product & Refractory Mfg
- 327210 Glass & Glass Product Mfg
- 327300 Cement & Concrete Product Mfg
- 327400 Lime & Gypsum Product Mfg
- 327900 Other Nonmetallic Mineral Product Mfg

### Code

#### Primary Metal Manufacturing

- 331110 Iron & Steel Mills & Ferroalloy Mfg
- 331200 Steel Product Mfg from Purchased Steel
- 331310 Alumina & Aluminum Production & Processing
- 331400 Nonferrous Metal (except Aluminum) Production & Processing
- 331500 Foundries

#### Fabricated Metal Product Manufacturing

- 332110 Forging & Stamping
- 332210 Cutlery & Handtool Mfg
- 332300 Architectural & Structural Metals Mfg
- 332400 Boiler, Tank, & Shipping Container Mfg
- 332510 Hardware Mfg
- 332610 Spring & Wire Product Mfg
- 332700 Machine Shops; Turned Product; & Screw, Nut, & Bolt Mfg
- 332810 Coating, Engraving, Heat Treating, & Allied Activities
- 332900 Other Fabricated Metal Product Mfg

#### Machinery Manufacturing

- 333100 Agriculture, Construction, & Mining Machinery Mfg
- 333200 Industrial Machinery Mfg
- 333310 Commercial & Service Industry Machinery Mfg
- 333410 Ventilation, Heating, Air-Conditioning, & Commercial Refrigeration Equipment Mfg
- 333510 Metalworking Machinery Mfg
- 333610 Engine, Turbine & Power Transmission Equipment Mfg
- 333900 Other General Purpose Machinery Mfg

#### Computer and Electronic Product Manufacturing

- 334110 Computer & Peripheral Equipment Mfg
- 334200 Communications Equipment Mfg
- 334310 Audio & Video Equipment Mfg
- 334410 Semiconductor & Other Electronic Component Mfg
- 334500 Navigational, Measuring, Electromedical, & Control Instruments Mfg
- 334610 Manufacturing & Reproducing Magnetic & Optical Media

#### Electrical Equipment, Appliance, and Component Manufacturing

- 335100 Electric Lighting Equipment Mfg
- 335200 Household Appliance Mfg
- 335310 Electrical Equipment Mfg
- 335900 Other Electrical Equipment & Component Mfg

#### Transportation Equipment Manufacturing

- 336100 Motor Vehicle Mfg
- 336210 Motor Vehicle Body & Trailer Mfg
- 336300 Motor Vehicle Parts Mfg
- 336410 Aerospace Product & Parts Mfg
- 336510 Railroad Rolling Stock Mfg
- 336610 Ship & Boat Building
- 336990 Other Transportation Equipment Mfg

#### Furniture and Related Product Manufacturing

- 337000 Furniture & Related Product Manufacturing



<p><b>Code</b></p> <p><b>Miscellaneous Manufacturing</b></p> <p>339110 Medical Equipment &amp; Supplies Mfg</p> <p>339900 Other Miscellaneous Manufacturing</p>	<p><b>Code</b></p> <p><b>Electronics and Appliance Stores</b></p> <p>443111 Household Appliance Stores</p> <p>443112 Radio, Television, &amp; Other Electronics Stores</p> <p>443120 Computer &amp; Software Stores</p> <p>443130 Camera &amp; Photographic Supplies Stores</p>	<p><b>Code</b></p> <p><b>Nonstore Retailers</b></p> <p>454110 Electronic Shopping &amp; Mail-Order Houses</p> <p>454210 Vending Machine Operators</p> <p>454311 Heating Oil Dealers</p> <p>454312 Liquefied Petroleum Gas (Bottled Gas) Dealers</p> <p>454319 Other Fuel Dealers</p> <p>454390 Other Direct Selling Establishments (including door-to-door retailing, frozen food plan providers, party plan merchandisers, &amp; coffee-break service providers)</p>	<p><b>Code</b></p> <p><b>Broadcasting (except Internet)</b></p> <p>515100 Radio &amp; Television Broadcasting</p> <p>515210 Cable &amp; Other Subscription Programming</p>
<p><b>Wholesale Trade</b></p> <p><b>Merchant Wholesalers, Durable Goods</b></p> <p>423100 Motor Vehicle &amp; Motor Vehicle Parts &amp; Supplies</p> <p>423200 Furniture &amp; Home Furnishings</p> <p>423300 Lumber &amp; Other Construction Materials</p> <p>423400 Professional &amp; Commercial Equipment &amp; Supplies</p> <p>423500 Metal &amp; Mineral (except Petroleum)</p> <p>423600 Electrical &amp; Electronic Goods</p> <p>423700 Hardware, &amp; Plumbing &amp; Heating Equipment &amp; Supplies</p> <p>423800 Machinery, Equipment, &amp; Supplies</p> <p>423910 Sporting &amp; Recreational Goods &amp; Supplies</p> <p>423920 Toy &amp; Hobby Goods &amp; Supplies</p> <p>423930 Recyclable Materials</p> <p>423940 Jewelry, Watch, Precious Stone, &amp; Precious Metals</p> <p>423990 Other Miscellaneous Durable Goods</p>	<p><b>Building Material and Garden Equipment and Supplies Dealers</b></p> <p>444110 Home Centers</p> <p>444120 Paint &amp; Wallpaper Stores</p> <p>444130 Hardware Stores</p> <p>444190 Other Building Material Dealers</p> <p>444200 Lawn &amp; Garden Equipment &amp; Supplies Stores</p> <p><b>Food and Beverage Stores</b></p> <p>445110 Supermarkets and Other Grocery (except Convenience) Stores</p> <p>445120 Convenience Stores</p> <p>445210 Meat Markets</p> <p>445220 Fish &amp; Seafood Markets</p> <p>445230 Fruit &amp; Vegetable Markets</p> <p>445291 Baked Goods Stores</p> <p>445292 Confectionery &amp; Nut Stores</p> <p>445299 All Other Specialty Food Stores</p> <p>445310 Beer, Wine, &amp; Liquor Stores</p> <p><b>Health and Personal Care Stores</b></p> <p>446110 Pharmacies &amp; Drug Stores</p> <p>446120 Cosmetics, Beauty Supplies, &amp; Perfume Stores</p> <p>446130 Optical Goods Stores</p> <p>446190 Other Health &amp; Personal Care Stores</p> <p><b>Gasoline Stations</b></p> <p>447100 Gasoline Stations (including convenience stores with gas)</p>	<p><b>Transportation and Warehousing</b></p> <p><b>Air, Rail, and Water Transportation</b></p> <p>481000 Air Transportation</p> <p>482110 Rail Transportation</p> <p>483000 Water Transportation</p> <p><b>Truck Transportation</b></p> <p>484110 General Freight Trucking, Local</p> <p>484120 General Freight Trucking, Long-distance</p> <p>484200 Specialized Freight Trucking</p> <p><b>Transit and Ground Passenger Transportation</b></p> <p>485110 Urban Transit Systems</p> <p>485210 Interurban &amp; Rural Bus Transportation</p> <p>485310 Taxi Service</p> <p>485320 Limousine Service</p> <p>485410 School &amp; Employee Bus Transportation</p> <p>485510 Charter Bus Industry</p> <p>485990 Other Transit &amp; Ground Passenger Transportation</p> <p><b>Pipeline Transportation</b></p> <p>486000 Pipeline Transportation</p> <p><b>Scenic &amp; Sightseeing Transportation</b></p> <p>487000 Scenic &amp; Sightseeing Transportation</p>	<p><b>Internet Publishing and Broadcasting</b></p> <p>516110 Internet Publishing &amp; Broadcasting</p> <p><b>Telecommunications</b></p> <p>517000 Telecommunications (including paging, cellular, satellite, cable &amp; other program distribution, resellers, &amp; other telecommunications)</p> <p><b>Internet Service Providers, Web Search Portals, and Data Processing Services</b></p> <p>518111 Internet Service Providers</p> <p>518112 Web Search Portals</p> <p>518210 Data Processing, Hosting, &amp; Related Services</p> <p><b>Other Information Services</b></p> <p>519100 Other Information Services (including news syndicates &amp; libraries)</p>
<p><b>Merchant Wholesalers, Nondurable Goods</b></p> <p>424100 Paper &amp; Paper Products</p> <p>424210 Drugs &amp; Druggists' Sundries</p> <p>424300 Apparel, Piece Goods, &amp; Notions</p> <p>424400 Grocery &amp; Related Products</p> <p>424500 Farm Product Raw Materials</p> <p>424600 Chemical &amp; Allied Products</p> <p>424700 Petroleum &amp; Petroleum Products</p> <p>424800 Beer, Wine, &amp; Distilled Alcoholic Beverages</p> <p>424910 Farm Supplies</p> <p>424920 Book, Periodical, &amp; Newspapers</p> <p>424930 Flower, Nursery Stock, &amp; Florists' Supplies</p> <p>424940 Tobacco &amp; Tobacco Products</p> <p>424950 Paint, Varnish, &amp; Supplies</p> <p>424990 Other Miscellaneous Nondurable Goods</p>	<p><b>Clothing and Clothing Accessories Stores</b></p> <p>448110 Men's Clothing Stores</p> <p>448120 Women's Clothing Stores</p> <p>448130 Children's &amp; Infants' Clothing Stores</p> <p>448140 Family Clothing Stores</p> <p>448150 Clothing Accessories Stores</p> <p>448190 Other Clothing Stores</p> <p>448210 Shoe Stores</p> <p>448310 Jewelry Stores</p> <p>448320 Luggage &amp; Leather Goods Stores</p> <p><b>Sporting Goods, Hobby, Book, and Music Stores</b></p> <p>451110 Sporting Goods Stores</p> <p>451120 Hobby, Toy, &amp; Game Stores</p> <p>451130 Sewing, Needlework, &amp; Piece Goods Stores</p> <p>451140 Musical Instrument &amp; Supplies Stores</p> <p>451211 Book Stores</p> <p>451212 News Dealers &amp; Newsstands</p> <p>451220 Pre-recorded Tape, Compact Disc, &amp; Record Stores</p>	<p><b>Support Activities for Transportation</b></p> <p>488100 Support Activities for Air Transportation</p> <p>488210 Support Activities for Rail Transportation</p> <p>488300 Support Activities for Water Transportation</p> <p>488410 Motor Vehicle Towing</p> <p>488490 Other Support Activities for Road Transportation</p> <p>488510 Freight Transportation Arrangement</p> <p>488990 Other Support Activities for Transportation</p> <p><b>Couriers and Messengers</b></p> <p>492110 Couriers</p> <p>492210 Local Messengers &amp; Local Delivery</p> <p><b>Warehousing and Storage</b></p> <p>493100 Warehousing &amp; Storage (except lessors of miniwarehouses &amp; self-storage units)</p>	<p><b>Finance and Insurance</b></p> <p><b>Depository Credit Intermediation</b></p> <p>522110 Commercial Banking</p> <p>522120 Savings Institutions</p> <p>522130 Credit Unions</p> <p>522190 Other Depository Credit Intermediation</p> <p><b>Nondepository Credit Intermediation</b></p> <p>522210 Credit Card Issuing</p> <p>522220 Sales Financing</p> <p>522291 Consumer Lending</p> <p>522292 Real Estate Credit (including mortgage bankers &amp; originators)</p> <p>522293 International Trade Financing</p> <p>522294 Secondary Market Financing</p> <p>522298 All Other Nondepository Credit Intermediation</p>
<p><b>Wholesale Electronic Markets and Agents and Brokers</b></p> <p>425110 Business to Business Electronic Markets</p> <p>425120 Wholesale Trade Agents &amp; Brokers</p>	<p><b>General Merchandise Stores</b></p> <p>452110 Department Stores</p> <p>452900 Other General Merchandise Stores</p>	<p><b>Information</b></p> <p><b>Publishing Industries (except Internet)</b></p> <p>511110 Newspaper Publishers</p> <p>511120 Periodical Publishers</p> <p>511130 Book Publishers</p> <p>511140 Directory &amp; Mailing List Publishers</p> <p>511190 Other Publishers</p> <p>511210 Software Publishers</p>	<p><b>Activities Related to Credit Intermediation</b></p> <p>522300 Activities Related to Credit Intermediation (including loan brokers, check clearing, &amp; money transmitting)</p>
<p><b>Retail Trade</b></p> <p><b>Motor Vehicle and Parts Dealers</b></p> <p>441110 New Car Dealers</p> <p>441120 Used Car Dealers</p> <p>441210 Recreational Vehicle Dealers</p> <p>441221 Motorcycle Dealers</p> <p>441222 Boat Dealers</p> <p>441229 All Other Motor Vehicle Dealers</p> <p>441300 Automotive Parts, Accessories, &amp; Tire Stores</p>	<p><b>Miscellaneous Store Retailers</b></p> <p>453110 Florists</p> <p>453210 Office Supplies &amp; Stationery Stores</p> <p>453220 Gift, Novelty, &amp; Souvenir Stores</p> <p>453310 Used Merchandise Stores</p> <p>453910 Pet &amp; Pet Supplies Stores</p> <p>453920 Art Dealers</p> <p>453930 Manufactured (Mobile) Home Dealers</p> <p>453990 All Other Miscellaneous Store Retailers (including tobacco, candle, &amp; trophy shops)</p>	<p><b>Motion Picture and Sound Recording Industries</b></p> <p>512100 Motion Picture &amp; Video Industries (except video rental)</p> <p>512200 Sound Recording Industries</p>	<p><b>Securities, Commodity Contracts, and Other Financial Investments and Related Activities</b></p> <p>523110 Investment Banking &amp; Securities Dealing</p> <p>523120 Securities Brokerage</p> <p>523130 Commodity Contracts Dealing</p> <p>523140 Commodity Contracts Brokerage</p> <p>523210 Securities &amp; Commodity Exchanges</p> <p>523900 Other Financial Investment Activities (including portfolio management &amp; investment advice)</p>
<p><b>Furniture and Home Furnishings Stores</b></p> <p>442110 Furniture Stores</p> <p>442210 Floor Covering Stores</p> <p>442291 Window Treatment Stores</p> <p>442299 All Other Home Furnishings Stores</p>			<p><b>Insurance Carriers and Related Activities</b></p> <p>524140 Direct Life, Health, &amp; Medical Insurance &amp; Reinsurance Carriers</p> <p>524150 Direct Insurance &amp; Reinsurance (except Life, Health &amp; Medical) Carriers</p> <p>524210 Insurance Agencies &amp; Brokerages</p> <p>524290 Other Insurance Related Activities (including third-party administration of insurance and pension funds)</p>

<p><b>Code</b> <b>Funds, Trusts, and Other Financial Vehicles</b> 525100 Insurance &amp; Employee Benefit Funds 525910 Open-End Investment Funds (Form 1120-RIC) 525920 Trusts, Estates, &amp; Agency Accounts 525930 Real Estate Investment Trusts (Form 1120-REIT) 525990 Other Financial Vehicles (including closed-end investment funds) "Offices of Bank Holding Companies" and "Offices of Other Holding Companies" are located under <b>Management of Companies (Holding Companies)</b> below.</p>	<p><b>Code</b> <b>Specialized Design Services</b> 541400 Specialized Design Services (including interior, industrial, graphic, &amp; fashion design) <b>Computer Systems Design and Related Services</b> 541511 Custom Computer Programming Services 541512 Computer Systems Design Services 541513 Computer Facilities Management Services 541519 Other Computer Related Services <b>Other Professional, Scientific, and Technical Services</b> 541600 Management, Scientific, &amp; Technical Consulting Services 541700 Scientific Research &amp; Development Services 541800 Advertising &amp; Related Services 541910 Marketing Research &amp; Public Opinion Polling 541920 Photographic Services 541930 Translation &amp; Interpretation Services 541940 Veterinary Services 541990 All Other Professional, Scientific, &amp; Technical Services</p>	<p><b>Code</b> <b>Health Care and Social Assistance</b> <b>Offices of Physicians and Dentists</b> 621111 Offices of Physicians (except mental health specialists) 621112 Offices of Physicians, Mental Health Specialists 621210 Offices of Dentists <b>Offices of Other Health Practitioners</b> 621310 Offices of Chiropractors 621320 Offices of Optometrists 621330 Offices of Mental Health Practitioners (except Physicians) 621340 Offices of Physical, Occupational &amp; Speech Therapists, &amp; Audiologists 621391 Offices of Podiatrists 621399 Offices of All Other Miscellaneous Health Practitioners <b>Outpatient Care Centers</b> 621410 Family Planning Centers 621420 Outpatient Mental Health &amp; Substance Abuse Centers 621491 HMO Medical Centers 621492 Kidney Dialysis Centers 621493 Freestanding Ambulatory Surgical &amp; Emergency Centers 621498 All Other Outpatient Care Centers</p>	<p><b>Code</b> 713900 Other Amusement &amp; Recreation Industries (including golf courses, skiing facilities, marinas, fitness centers, &amp; bowling centers) <b>Accommodation and Food Services</b> <b>Accommodation</b> 721110 Hotels (except Casino Hotels) &amp; Motels 721120 Casino Hotels 721191 Bed &amp; Breakfast Inns 721199 All Other Traveler Accommodation 721210 RV (Recreational Vehicle) Parks &amp; Recreational Camps 721310 Rooming &amp; Boarding Houses <b>Food Services and Drinking Places</b> 722110 Full-Service Restaurants 722210 Limited-Service Eating Places 722300 Special Food Services (including food service contractors &amp; caterers) 722410 Drinking Places (Alcoholic Beverages)</p>
<p><b>Real Estate and Rental and Leasing</b> <b>Real Estate</b> 531110 Lessors of Residential Buildings &amp; Dwellings 531114 Cooperative Housing 531120 Lessors of Nonresidential Buildings (except Miniwarehouses) 531130 Lessors of Miniwarehouses &amp; Self-Storage Units 531190 Lessors of Other Real Estate Property 531210 Offices of Real Estate Agents &amp; Brokers 531310 Real Estate Property Managers 531320 Offices of Real Estate Appraisers 531390 Other Activities Related to Real Estate</p>	<p><b>Management of Companies (Holding Companies)</b> 551111 Offices of Bank Holding Companies 551112 Offices of Other Holding Companies</p>	<p><b>Medical and Diagnostic Laboratories</b> 621510 Medical &amp; Diagnostic Laboratories <b>Home Health Care Services</b> 621610 Home Health Care Services</p>	<p><b>Other Services</b> <b>Repair and Maintenance</b> 811110 Automotive Mechanical &amp; Electrical Repair &amp; Maintenance 811120 Automotive Body, Paint, Interior, &amp; Glass Repair 811190 Other Automotive Repair &amp; Maintenance (including oil change &amp; lubrication shops &amp; car washes) 811210 Electronic &amp; Precision Equipment Repair &amp; Maintenance 811310 Commercial &amp; Industrial Machinery &amp; Equipment (except Automotive &amp; Electronic) Repair &amp; Maintenance 811410 Home &amp; Garden Equipment &amp; Appliance Repair &amp; Maintenance 811420 Reupholstery &amp; Furniture Repair 811430 Footwear &amp; Leather Goods Repair 811490 Other Personal &amp; Household Goods Repair &amp; Maintenance</p>
<p><b>Rental and Leasing Services</b> 532100 Automotive Equipment Rental &amp; Leasing 532210 Consumer Electronics &amp; Appliances Rental 532220 Formal Wear &amp; Costume Rental 532230 Video Tape &amp; Disc Rental 532290 Other Consumer Goods Rental 532310 General Rental Centers 532400 Commercial &amp; Industrial Machinery &amp; Equipment Rental &amp; Leasing <b>Lessors of Nonfinancial Intangible Assets (except copyrighted works)</b> 533110 Lessors of Nonfinancial Intangible Assets (except copyrighted works)</p>	<p><b>Administrative and Support and Waste Management and Remediation Services</b> <b>Administrative and Support Services</b> 561110 Office Administrative Services 561210 Facilities Support Services 561300 Employment Services 561410 Document Preparation Services 561420 Telephone Call Centers 561430 Business Service Centers (including private mail centers &amp; copy shops) 561440 Collection Agencies 561450 Credit Bureaus 561490 Other Business Support Services (including repossession services, court reporting, &amp; stenotype services) 561500 Travel Arrangement &amp; Reservation Services 561600 Investigation &amp; Security Services 561710 Exterminating &amp; Pest Control Services 561720 Janitorial Services 561730 Landscaping Services 561740 Carpet &amp; Upholstery Cleaning Services 561790 Other Services to Buildings &amp; Dwellings 561900 Other Support Services (including packaging &amp; labeling services, &amp; convention &amp; trade show organizers)</p>	<p><b>Other Ambulatory Health Care Services</b> 621900 Other Ambulatory Health Care Services (including ambulance services &amp; blood &amp; organ banks) <b>Hospitals</b> 622000 Hospitals <b>Nursing and Residential Care Facilities</b> 623000 Nursing &amp; Residential Care Facilities <b>Social Assistance</b> 624100 Individual &amp; Family Services 624200 Community Food &amp; Housing, &amp; Emergency &amp; Other Relief Services 624310 Vocational Rehabilitation Services 624410 Child Day Care Services</p>	<p><b>Personal and Laundry Services</b> 812111 Barber Shops 812112 Beauty Salons 812113 Nail Salons 812190 Other Personal Care Services (including diet &amp; weight reducing centers) 812210 Funeral Homes &amp; Funeral Services 812220 Cemeteries &amp; Crematories 812310 Coin-Operated Laundries &amp; Drycleaners 812320 Drycleaning &amp; Laundry Services (except Coin-Operated) 812330 Linen &amp; Uniform Supply 812910 Pet Care (except Veterinary) Services 812920 Photofinishing 812930 Parking Lots &amp; Garages 812990 All Other Personal Services</p>
<p><b>Professional, Scientific, and Technical Services</b> <b>Legal Services</b> 541110 Offices of Lawyers 541190 Other Legal Services <b>Accounting, Tax Preparation, Bookkeeping, and Payroll Services</b> 541211 Offices of Certified Public Accountants 541213 Tax Preparation Services 541214 Payroll Services 541219 Other Accounting Services <b>Architectural, Engineering, and Related Services</b> 541310 Architectural Services 541320 Landscape Architecture Services 541330 Engineering Services 541340 Drafting Services 541350 Building Inspection Services 541360 Geophysical Surveying &amp; Mapping Services 541370 Surveying &amp; Mapping (except Geophysical) Services 541380 Testing Laboratories</p>	<p><b>Waste Management and Remediation Services</b> 562000 Waste Management &amp; Remediation Services <b>Educational Services</b> 611000 Educational Services (including schools, colleges, &amp; universities)</p>	<p><b>Arts, Entertainment, and Recreation</b> <b>Performing Arts, Spectator Sports, and Related Industries</b> 711100 Performing Arts Companies 711210 Spectator Sports (including sports clubs &amp; racetracks) 711300 Promoters of Performing Arts, Sports, &amp; Similar Events 711410 Agents &amp; Managers for Artists, Athletes, Entertainers, &amp; Other Public Figures 711510 Independent Artists, Writers, &amp; Performers <b>Museums, Historical Sites, and Similar Institutions</b> 712100 Museums, Historical Sites, &amp; Similar Institutions <b>Amusement, Gambling, and Recreation Industries</b> 713100 Amusement Parks &amp; Arcades 713200 Gambling Industries</p>	<p><b>Religious, Grantmaking, Civic, Professional, and Similar Organizations</b> 813000 Religious, Grantmaking, Civic, Professional, &amp; Similar Organizations (including condominium and homeowners associations)</p>

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