LGS

Additional information for Investors

Definition of Passive vs Active Investor

- Related businesses that form an appropriate economic unit are treated as a single “activity”. Related businesses conducted via a Schedule C, partnership, C or S Corporation, or limited liability company may be grouped into one activity. An “activity” is not constrained by entity lines. [Reg. § 1.469-4(c) and 1.469- 4(d)(4)]

- A trade or businesses is a passive activity if the taxpayer does not materially participate. The taxpayer materially participates if and only if he or she meets **one** of the following seven tests provided [Reg. § 1.469-5T(a)]

    1. **The taxpayer works 500 hours or more during the year in the activity.**
    2. The taxpayer does substantially all the work in the activity.
    3. The taxpayer works more than 100 hours in the activity during the year and no one else works more than the taxpayer.
    4. The activity is a significant participation activity (SPA), and the sum of SPAs in which the taxpayer works 100-500 hours exceeds 500 hours for the year.
    5. The taxpayer materially participated in the activity in any 5 of the prior 10 years.
    6. The activity is a personal service activity and the taxpayer materially participated in that activity in any 3 prior years.
    7. Based on all of the facts and circumstances, the taxpayer participates in the activity on a regular, continuous, and substantial basis during such year. However, this test only applies if the taxpayer works at least 100 hours in the activity, no one else works more hours than the taxpayer in the activity, and no one else receives compensation for managing the activity.

Note: The first four tests look to a set number of hours of participation in the tax year. The next two tests look to material participation in prior tax years. The final test looks to the facts and circumstances, but is highly restrictive

Composite Returns

All former Axios investors will have the option in 2017 of being included on a composite return even though they received state K-1s in 2016

If the LGS investor elects to be included in the 2017 composite return, their capital account will be reduced by any state tax paid on their behalf

States have different rules on loss carryforwards but generally on an individual tax return, states do allow losses to be applied from 2016 to taxable income of a future year (there is generally no concept of state loss carryforwards on composite returns).

LGS investors should speak to their tax adviser regarding pros/cons of being included in a composite return in 2017.

Example of Capital Account Rollforward

	Legacy	New
Number of Units	25,000	25,000
$5.50 Legacy & $8.50 Axios	137,500	212,500
2016 Income Allocation Example		
Income Allocated Prorata	2,000,000	2,000,000
2016 Income Allocation to adjust capital accounts	**37,500**	**(37,500)**
Adjusted Ending Capital	2,175,000	2,175,000
2016 Distribution	(5,000)	(5,000)
2016 Extra Distribution for taxes paid	(5,000)	
Ending Capital - 12/31/2016	2,165,000	2,170,000
2017 Income	100,000	100,000
Tax Paid on Composite (Legacy taxpayer elects not to join composite)	-	(15,000)
Tax Gain on Sale	2,935,000	2,935,000
Final Distribution	**(5,200,000)**	**(5,190,000)**
Final Capital After Sale	**-**	**-**

Schedule K-1 – Part J Computation

The number of units bought by each partner has not changed even though it may look like that on Schedule K-1 Box J.

Axios partners joined the Legos Holdings partnership on 09/30/2015. Since the partners joined the partnership during the tax year, a formula is used to compute the pro-rated partners' ownership percentage for the year using the number of days remaining from 09/30/2015 to 12/31/2015 (92 days) and the formula is - **Number of Units Bought by a Partner/Total Number of Units)*92/365.**

For 2016, the ownership percentages were calculated for the whole year by dividing number of units for each partner by total number of units. As such, there is a change between beginning ownership percentage and ending ownership percentage on Schedule K-1 Box J.