



# **FEDERAL BAR ASSOCIATION 2009 TAX LAW CONFERENCE**

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# Topics

- **§457A – Partnership Tax Aspects**
- **§108(e)(8) – Partnership Debt For Equity**
- **§704(c)(1)(C) – Contribution of Built-In Loss Property**
- **Series LLCs**
- **Fannie – Freddie Rev. Proc.**
- **Business Plan**

# Section 108(e)(8)

Selected issues

# Section 108(e)(8)

## **Indebtedness satisfied by corporate stock or partnership interest.**

For purposes of determining income of a debtor from discharge of indebtedness, if—

- (A) a debtor corporation transfers stock, or
- (B) a debtor partnership transfers a capital or profits interest in such partnership,

to a creditor in satisfaction of its recourse or nonrecourse indebtedness, such corporation or partnership shall be treated as having satisfied the indebtedness with an amount of money equal to the fair market value of the stock or interest. In the case of any partnership, any discharge of indebtedness income recognized under this paragraph shall be included in the distributive shares of taxpayers which were the partners in the partnership immediately before such discharge.

## Section 108(e)(8)

- Should the contributing partner be entitled to a bad-debt deduction?
  - Failure to allow may result in lack of parity (income to one party, no loss to the other).
  - Differing treatment would place a premium on tax planning.

## Section 108(e)(8)

- Will the rules of Section 108(e)(8) be coordinated with those of 704(c)(1)(C), since both generally involve the contribution of a built-in loss asset?
  - Would consideration be given to adopting, for purposes of Section 108, the suspended loss account approach?
  - The suspended loss rule would be at odds with the approach adopted by the Section 108 proposed regulations.

## Section 108(e)(8)

- Regarding the allocation of COD income recognized under Section 108(e)(8):
  - Should it be allocated to the creditor if that person is also a partner?
  - Should the income be treated as a Treas. Reg. §1.704-2(f)(6) first-tier item?



## Section 108(e)(8)

- How will the non-comp option rules on convertible debt interact with these rules?

# Section 108(i)

Selected issues

# Section 108(i) Background

- Corporate debtors or debt incurred “in connection with” trade or business
- Elective
- Limited window – 2009 and 2010 cancellations
- OID and AHYDO implications
- Acceleration rules
- Special partnership rules apply
- Many unanswered questions

# Section 108(i)

## Partnership issues

- Determination of “in connection with”
  - Applied at partnership level?
  - Aggregate principles to apply for corporate partners?
  - Tracing of debt
    - Debt-financed contributions
    - Debt-financed distributions
    - Debt-financed buyouts

# Section 108(i)

## Partnership issues

- Acceleration events:
  - Technical terminations?
  - Partnership mergers?
  - Partnership incorporations?
  - Calculation of partial sale or liquidation
  - Distributions?

# Section 704(c)(1)(C)

Selected issues

## Section 704(c)(1)(C)

- Did Congress intend to (at least partially) repeal the ceiling rule?
- Example:
  - A contributes property with FMV of \$50, AB of \$100.
  - Property increases in value and is sold for \$60.
  - Should the other partners benefit from the higher basis (hence no gain), or is their gain computed by reference to a \$50 basis?

## Section 704(c)(1)(C)

- Should the outside basis of a 704(c)(1)(C) contributing partner reflect the excess basis contributed?
- Consideration was given to creating a suspended loss account.
  - Overly complex
  - Extra-statutory
  - Inconsistent with other sub K provisions



## Section 704(c)(1)(C)

- Assuming the partner's outside basis reflects the basis of the contributed property:
  - Will the property's basis be decreased as the partner's basis in the partnership interest is decreased?
  - Or, should the basis of the partnership's property be unaffected by reductions in partnership interest basis?

## Section 704(c)(1)(C)

- Does 704(c)(1)(C) only apply to forward built-in loss items?
  - Section 704(c)(1)(A) applies to forward and reverse Section 704(c) items.
  - Section 704(c)(1)(B) only applies to forward Section 704(c) items.

## Section 704(c)(1)(C)

- Will a non-Section 381 step-in-the-shoes rule apply?
  - For example, will the partners of a non-continuing partnership in a partnership merger lose the built-in-loss benefit upon the termination of the transferor?
  - A similar issue arises in a partnership technical termination.

# Series LLCs – What Are They?

- Delaware created first “series LLC” or “protected cell company” in 1996. Since then Illinois, Iowa, Nevada, Oklahoma, Tennessee and Utah have adopted similar legislation.
- Delaware allows each series to:
  - Have separate business; separate members;
  - Have separate property rights; separate profit and loss sharing from such property;
  - Limit debt enforceability to assets of each series; and
  - Contract, hold title, and grant liens separately.

# Series LLCs – What Are The Tax Questions?

- Is each Series a separate Business Entity?
- Is the LLC that owns the series a separate Business Entity?
- If a separate Business Entity, is it an “eligible entity”?
- Because state statutes vary, should the regime be elective, include default treatment, or be based on a Kintner-type of analysis (i.e., pre check-the-box multiple factors test)?

# Series LLCs – Tax Differences if Treat as Single vs. Multiple Entities

- Tax return filing obligations
- Capitalization of organizational costs for each series? Reg. § 1.263(a)-5(a)(6); § 195
- Section 752 debt allocations and non-recourse deduction allocations
- Cross movement of assets among series
- Book up events effecting single series entity vs. all series
- Treatment of distributions that liquidate interest in only one of several series

# Series LLCs – Guidance to Date

- Notice 2008-19 asked for comments
- PLR 200803004 treats each series as separate business entity
- MA letter ruling treated Del. Series LLC as creating multiple business entities
- CA Franchise Board treats each series as a separate business entity
- Analogous non-series authorities support separate entity treatment: *National Securities Series – Industrial Stock Series v. Comm’r*; *Rev. Rul. 55-39 and Rev. Rul. 55-416*

# Series LLCs – ABA Recommendation

- Prospective guidance should treat each series as a separate business entity
- Prospective guidance should treat overall LLC as disregarded entity if no separate assets or liabilities
- Each series would be an “eligible entity” defaulting as partnership or disregarded entity depending on the number of members
- Suggestion based on Delaware model statute



# IRS-Treasury Business Plan

- **PARTNERSHIP RELATED GUIDANCE PROJECTS ON THE 2008/2009 GUIDANCE PRIORITY LIST**
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- **1. Series LLC's Proposed Regulation**
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- **2. § 704(c) Mergers Final Regulations**
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- **3. § 704(c)(1)(C)/743(b)/734(b) Jobs Act Proposed Regulation**
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- **4. § 704 (c) Remedial Final Regulation**
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- **5. § 704(b) Related Party Substantiality Proposed Regulation**
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- **6. § 706 Varying Interest Proposed Regulation**
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- **7. § 721 Partnership Equity for Services Proposed Regulation**

# IRS-Treasury Business Plan

- **PARTNERSHIP RELATED GUIDANCE PROJECTS ON THE 2008/2009 GUIDANCE PRIORITY LIST**
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- **8. § 721 Noncompensatory Partnership Options**
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- **9. §§ 704/465 DRO and At-Risk “Hubert” Final Regulations**
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- **10. §108 (e)(8) Partnership Equity for Debt Final Regulations**
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- **11. § 707 Disguised Sale Proposed Regulations (Withdrawn)**
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- **12. § 751 Unrealized Receivables Proposed Regulations**
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- **13. §761(f) Qualified Spousal Joint Ventures Proposed Regulations**
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- **14. § 469 Grouping Rev. Proc.**
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- **15. § 7701 Extensions of Time to File Entity Classification Elections**