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The Limited Partnership with a Corporate General Partner - Federal Taxation - Partnership of Association

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Recently there has been an increasing number of limited partnerships formed with a corporation as the sole general partner. This arrangement combines primary advantages of both the partnership and the corporation—direct receipt of profits and losses by the partners without taxation at the organizational level, and limited liability for all members of the organization. There is some doubt, however, that this type of organization will be treated for tax purposes as a partnership. An indication of the uncertainty is the following statement published in a prospectus offering limited partnership shares to the public:

There is no guaranty that the Internal Revenue Code or the regulations promulgated thereunder will not further be amended in such a manner as to deprive the Partnership and the Partners of any tax benefits prospective investors in the Partnership may contemplate. If for any reason the Partnership is treated for tax purposes as an association taxable as a corporation rather than a partnership, the Partnership will be required to pay taxes upon its income, distributions to Partners may be taxable to such Partners and will not be deductible in computing the Partnership’s taxable income and, in addition, interest paid on the Partnership’s obligations, depreciation taken on Partnership properties and other deductible items will be deductible only by the Partnership rather than being passed through to the Partners.

No doubt the necessity for this caveat is created by the concern of the Internal Revenue Service over the increased use of the limited partnership with a corporate general partner. In the past, limited partnerships have been used primarily as a means of affording investors limited liability without the formalities of incorporating. The classical concept of the limited partnership is that of a person or persons managing a business which is financed by someone who is merely an investor and does not participate in the management. The general partner has all the rights and powers and is subject to all the restrictions and liabilities of a partner in a general partnership. The limited partner has only the basic rights of being able to obtain full information about the partnership, to share in profits, and to have a dissolution and winding up by court decree when he is given the right to dissolve. Generally, a limited partner is only liable for part-

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1 As evidence of this, during the period from July 20 through September 20, 1969, 38% of the 121 limited partnership certificates filed with the Texas Secretary of State had a corporation as their sole general partner. Letter from Ivon Lee III, Counsel to the Secretary of State, to Mike Allison, Oct. 11, 1969. During the period from Jan. 1 through Feb. 28, 1970, 40% of the 141 limited partnerships filed in Texas had a corporate general partner. Letter from Donald W. Ray, Legal Counsel to the Secretary of State, to Mike Allison, Mar. 13, 1970.


3 Uniform Limited Partnership Act § 9.

4 Id. § 10.
nership debts to the extent of his capital contribution. However, he may be liable as a general partner under certain circumstances, for example, if he exercises control of the business. Limited liability is an attractive feature offered by both limited partnerships and corporations, but limited partnerships offer a tax feature unavailable to the corporation, which is subject to "double taxation.” In the partnership structure the partners are credited with the profits and losses of the business pro rata as individuals. This pass-through of profits and losses to the partners with no taxation at the organizational level is especially attractive in operations which generate large amounts of tax deductions. The main areas in which substantial deductions occur are in oil and gas operations, in which intangible drilling cost write-offs and percentage depletion are available, and in real estate development, in which accelerated depreciation is allowed. Although many of the tax benefits have been reduced by the Tax Reform Act of 1969, there are still sufficient tax advantages to make the use of limited partnerships attractive.

Regulations promulgated under the Internal Revenue Code provide that the manner in which a business organization will be taxed depends upon its classification as either an association, partnership, or trust, and not the name attributed to the organization by state law or by its owners. The

5 Id. § 17 (1).
6 Id. § 7. For other circumstances giving rise to unlimited liability, see text accompanying notes 77-79 infra.
7 INT. REV. CODE of 1954, § 11 imposes a tax on corporate income, and id. § 1 imposes a tax on individual income which, under id. § 61 (a) (7), includes dividends; hence the income of a corporation is taxed at the corporate level and again when it is distributed to the stockholders.
8 INT. REV. CODE of 1954, § 701. A 'Subchapter S Corporation,' provided for under id. §§ 1371-78, is taxed in a manner similar to a partnership, but qualifying corporations are limited to ten or less natural persons as stockholders and are subject to many restrictions.
9 Tax Reform Act of 1969, 83 Stat. 487 (codified in scattered sections of 26 U.S.C.). Among the benefits reduced are (1) limiting the use of double declining balance and sum of the years' digits methods of depreciation solely to new residential rental property, Tax Reform Act of 1969, § 521 (a), adding INT. REV. CODE of 1954, § 167 (j)-(l), relettering (j) as (m); (2) requiring 100% recapture of post-1969 excess depreciation on real property other than residential rental property, Tax Reform Act of 1969, § 521 (b), amending INT. REV. CODE of 1954, § 1250 (a); (3) limiting the deduction allowed individuals for interest on funds borrowed for investment purposes for taxable years beginning after Dec. 31, 1971, Tax Reform Act of 1969, § 221 (a), adding INT. REV. CODE of 1954, § 163 (d), relettering (d) as (e); (4) reducing the percentage depletion in oil and gas operations from 27%. to 22%, Tax Reform Act of 1969, § 501 (a), amending INT. REV. CODE of 1954, § 613 (b)(1); (5) increasing the alternative tax rate for net long-term capital gains for individuals, Tax Reform Act of 1969, § 511 (b), amending INT. REV. CODE of 1954, § 1201; (6) making all taxpayers liable for a minimum tax on tax preference items which include excess investment interest, accelerated depreciation, net lease—personal property, fast write-off for certified pollution control facilities and railroad rolling stock in excess of normal depreciation, stock options, bad debt deductions of financial institutions, excess of depletion allowable over adjusted basis of the property at year's end, Tax Reform Act of 1969, § 301 (a), adding INT. REV. CODE of 1954, §§ 56-58; (7) repealing the investment credit, Tax Reform Act of 1969, §§ 703 (a)-(c), amending INT. REV. CODE of 1954, §§ 46, 47, and adding § 49; (8) reducing the benefits of charitable contributions of appreciated property, Tax Reform Act of 1969, § 201, amending INT. REV. CODE of 1954, § 170; and (9) reducing the benefits from a bargain sale to charity, Tax Reform Act of 1969, § 201, amending INT. REV. CODE of 1954, § 1011.
10 The pass-through of partnership profits and losses to the partners is the primary attraction, but a partner is allowed a loss only to the extent of the adjusted basis of his partnership interests. INT. REV. CODE of 1954, § 704 (d). A partner can, however, increase the basis of his partnership interest by assuming a portion of the partnership liabilities, as this is considered a contribution of partnership under id. § 772 (a). Thus a partner can deduct a greater amount of loss than the investment that he makes in his partnership shares.
11 Treas. Reg. § 301.7701-1 (b) (1960).
Regulations establish the standards for determining the class in which an organization belongs, but local law governs as to whether the legal relationships which have been established in the formation of an organization are such that the standards are met. As a result, in order to determine the classification of an organization, it is necessary to closely examine applicable laws in the state where the organization is formed. Since limited partnerships, like corporations, are creatures of statutory law, both partnership and corporate laws must be examined to determine the proper tax classification of a limited partnership with a corporate general partner.

After describing the prevalent statutory schemes which govern limited partnerships with a corporate general partner, this Comment will discuss the various considerations which have been involved in classifying this type of organization, and will attempt to evaluate the unofficial position of the Internal Revenue Service.

I. STATE PARTNERSHIP AND CORPORATION LAWS

Power of a Corporation To Become a Partner. In most states, limited partnerships are governed by statutes based on the Uniform Limited Partnership Act (hereinafter referred to as ULPA) and the Uniform Partnership Act (hereinafter referred to as UPA). The ULPA defines a limited partnership as “a partnership formed by two or more persons... having as members one or more general partners and one or more limited partners.” The UPA, which applies to limited partnerships except where inconsistent with limited partnership provisions, defines “persons” to include individuals, partnerships, corporations, and other associations. No where does the ULPA disqualify a corporation from becoming a partner;

18 Id. § 301.7701-1(c).
14 6 Uniform Laws Annotated 519 (master ed. 1969) lists the 45 jurisdictions which have adopted the Act: Alaska (1917), Arizona (1941), Arkansas (1953), California (1949), Colorado (1931), Connecticut (1961), District of Columbia (1962), Florida (1941), Georgia (1952), Hawaii (1941), Idaho (1919), Illinois (1917), Indiana (1949), Iowa (1924), Kansas (1967), Maryland (1918), Massachusetts (1923), Michigan (1931), Minnesota (1919), Mississippi (1964), Missouri (1947), Montana (1947), Nebraska (1919), Nevada (1931), New Hampshire (1937), New Jersey (1919), New Mexico (1947), New York (1922), North Carolina (1941), North Dakota (1959), Ohio (1957), Oklahoma (1951), Pennsylvania (1917), Rhode Island (1930), South Carolina (1950), South Dakota (1925), Tennessee (1919), Texas (1955), Utah (1921), Vermont (1941), Virgin Islands (1957), Virginia (1918), Washington (1945), West Virginia (1953), and Wisconsin (1919).
15 Id. at 1 lists the 42 jurisdictions which have adopted the Act: Alaska (1917), Arizona (1941), Arkansas (1949), California (1949), Colorado (1911), Connecticut (1961), Delaware (1947), District of Columbia (1962), Idaho (1919), Illinois (1917), Indiana (1949), Kentucky (1954), Maryland (1916), Massachusetts (1922), Michigan (1917), Minnesota (1921), Missouri (1949), Montana (1947), Nebraska (1943), Nevada (1911), New Jersey (1919), New Mexico (1947), New York (1919), North Carolina (1941), North Dakota (1919), Ohio (1949), Oklahoma (1917), Oregon (1939), Pennsylvania (1915), Rhode Island (1937), South Carolina (1930), South Dakota (1933), Tennessee (1927), Texas (1961), Utah (1921), Vermont (1941), Virgin Islands (1957), Virginia (1918), Washington (1951), West Virginia (1953), Wisconsin (1915), and Wyoming (1917).
16 Uniform Limited Partnership Act § 1.
17 Uniform Partnership Act § 6(2). A Texas court of civil appeals specifically held that the provisions of the Texas Uniform Partnership Act are applicable to limited partnerships organized under the Texas Uniform Limited Partnership Act. Horn v. Builders Supply Co., 401 S.W.2d 143 (Tex. Civ. App. 1966), error ref. n.r.e.
18 Uniform Partnership Act § 3.
therefore, in states which have passed both uniform acts without modifying
the appropriate sections, or in states which have similar provisions and
definitions, corporations are not prohibited by partnership law from be-
coming either general or limited partners. A comment to the UPA points
out that the question of the capacity of a corporation to become a partner
is a matter of corporate law.

A great many of the courts which have considered the capacity of a
corporation to become a partner have adopted a rule that, unless expressly
authorized by statute or charter, corporations do not ordinarily have the
power to become partners. This general rule is based on two lines of
reasoning. One is that the mutual agency relation between partners, allow-
ing each to share in the management of the business, conflicts with the
statutory requirement of board of director control of corporate activi-
ties. The other rationale views management’s entrance into a partnership
arrangement as a move which subjects corporate assets to risks and liabilities
not contemplated by the stockholders at the time they invested. The
general rule seems to be designed to protect stockholders and not to pro-
hibit some violation of public policy concerning the partnership arrange-
ment itself. However, its prohibition does not apply in states which have
adopted the wording of the Model Business Corporation Act, because that
Act expressly authorizes a corporation’s participation in partnerships.
Texas, New York, and Delaware are among states which authorize cor-

\[\text{Footnotes:}\]

19 See Memphis Natural Gas Co. v. Bleder, 115 U.S. 649 (1942), aff'g sub nom. Memphis
National Gas Co. v. Pope, 178 Tenn. 580, 161 S.W.2d 211 (1941). States and territories which have
passed both the UPA and ULPA are as follows: Alaska, Arizona, Arkansas, California, Colorado,
Connecticut, Idaho, Illinois, Indiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri,
Montana, Nebraska, Nevada, New Jersey, New Mexico, New York, North Carolina, North Dakota,
Ohio, Oklahoma, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas,
Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, District of Columbia, and the
Virgin Islands. See notes 14 and 15 supra. Texas has passed the ULPA in substantially the same form
though Delaware has not adopted the ULPA, its partnership act is the same as the UPA as to
definitions. Del. Code Ann. tit. 6, §§ 1501, 1502 (1953). The limited partnership definitions are
also similar. Id. § 1506(b). Further, its limited partnership statutes do not disqualify corporations
from becoming partners. Id. §§ 1701-12. New York’s adaptations of the Uniform Acts do not
change the definition of "person." N.Y. PARTNERSHIP LAW § 2 (McKinney 1948). The application
of the partnership act to limited partnerships is also unchanged, and New York law does not
prohibit corporations from becoming partners. Id. § 10(2).

20 UNIFORM PARTNERSHIP ACT § 6(1), Comment.

21 In Luling Oil & Gas Co. v. Humble Oil & Ref. Co., 144 Tex. 473, 191 S.W.2d 716 (1945),
the Texas supreme court held that where a corporation’s charter does not permit the forming of
partnerships, it is against the public policy of the state for the corporation to enter into such a
relationship. This rule was reiterated in J. Robert Neal, Inc. v. McElveen, 320 S.W.2d 36 (Tex.
N.Y. Civ. Proc. 582, 24 N.E. 834 (Ct. App. 1890), and Frieda Popkov Corp. v. Stack, 198 Misc.
826, 103 N.Y.S.2d 507 (Sup. Ct. 1950). Other states which appear to follow this general rule are
Alabama, Arkansas, Arizona, California, Georgia, Hawaii, Illinois, Indiana, Kentucky, Louisiana,
Massachusetts, Michigan, Missouri, Nebraska, New Hampshire, Ohio, Oklahoma, Oregon, Pennyl-
svania, South Carolina, Tennessee, Virginia, and West Virginia. Annot., 60 A.L.R.2d 917, 920

1890); Sabine Tram Co. v. Bancroft, 16 Tex. Civ. App. 170, 40 S.W. 837 (1897), error ref.;

23 Port Arthur Trust Co. v. Muldrow, 155 Tex. 612, 291 S.W.2d 312 (1956); Annot., 60

porate participation in partnerships. It would seem that in states which have no statutory language either authorizing or prohibiting such participation, a corporate charter can provide the authorization. Where there is statutory language or charter authority, it is likely that a court would hold that a corporation could become a partner.

Although the reasons for the rule that prohibits a corporation from becoming a partner unless authorized by statute or charter have some relevance in situations involving general partnerships, they are not logically applicable to limited partnerships which have a corporation as the sole general partner. Where the corporation is the sole general partner, the management of the corporation is not shared by anyone other than the corporation's directors and shareholders because under the ULPA only the general partner has the right to manage the business. Since the corporation is the only "person" with the right to manage, its assets are not subjected to unanticipated risks created by the actions of other general partners.

Under many present state statutes, it is not difficult to form a limited partnership with a corporate general partner. For example, in Texas a corporation can be formed with a minimum capital of $1,000. Once the corporate charter is granted, a limited partnership certificate with the necessary data required, naming a corporation as the general partner, can be filed. In Port Arthur Trust Co. v. Muldrow, 155 Tex. 612, 291 S.W.2d 312 (1956), the Supreme Court of Texas issued a writ of mandamus ordering the Texas Secretary of State to receive and file a limited partnership certificate in which a corporation was to become a limited partner in a limited partnership involving trusts. The corporation's charter granted the right to act as trustee under any lawful express trust. The court held that prior to the new Corporation Code, a corporation could not enter into a partnership, but under a corporation statute that permitted a corporation to act as trustee and where the charter granted such power, it was legally qualified as a person to become a member of a limited partnership. Other states which appear to hold this view are California, Connecticut, Georgia, Hawaii, Indiana, Minnesota, North Carolina, Oregon, Tennessee, Utah, and Virginia. Annot., 60 A.L.R.2d 917, 920 (1958). See also Note, Corporations—Corporate Powers and Liabilities—Partnership—Power of a Corporation To Enter Into a Limited Partnership—Port Arthur Trust Co. v. Muldrow, 291 S.W.2d 312 (Tex. Sup. Ct. 1956), 35 Texas L. Rev. 265 (1957).

28 UNIFORM LIMITED PARTNERSHIP ACT § 9 gives the general partner all the rights and powers of a partner in a partnership without limited partners except for seven enumerated acts going to the basic structure of the partnership that cannot be done without authorization from the limited partners. Id. § 7 limits the liability of a limited partner only as long as he does not take part in the control of the business. See notes 77-80 infra, and accompanying text. It therefore seems reasonable that limited partners will not be sharing in the management of the partnership.

In fact, the situation is one in which the corporation exercises sole control over more assets than the stockholders may have contemplated.
be filed with the Secretary of State, together with a filing fee of $25. Following these formalities creates a valid limited partnership.

**Problem of Control.** Participation in the control of the business by a limited partner has long been a problem connected with limited partnerships because there is little guidance as to what degree of participation is necessary before a limited partner will be held liable as a general partner. California is the only state in which the state partnership act sets out a list of activities a limited partner may engage in without becoming a general partner. However, these permissible activities go to the very structure of

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<td>(G)</td>
<td>The additional contributions, if any, agreed to be made by each limited partner and the times at which or events on the happening of which they shall be made.</td>
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<td>(H)</td>
<td>The time, if agreed upon, when the contribution of each limited partner is to be returned.</td>
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<td>(I)</td>
<td>The share of the profits or the other compensation by way of income which each limited partner shall receive by reason of his contribution.</td>
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<td>(J)</td>
<td>The right, if given, of a limited partner to substitute an assignee as contributor in his place, and the terms and conditions of the substitution.</td>
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<td>(K)</td>
<td>The right, if given, of the partners to admit additional limited partners.</td>
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<td>(L)</td>
<td>The right, if given, of one or more of the limited partners as to contributions or as to compensation by way of income, and the nature of such priority.</td>
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<td>(M)</td>
<td>The right, if given, of the remaining general partner or partners to continue the business on the death, retirement or insanity of a general partner.</td>
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<tr>
<td>(N)</td>
<td>The right, if given, of a limited partner to demand and receive property other than cash in return for his contribution.</td>
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Id. § 3(a)(2).

Id. § 3(b). A limited partnership is formed if there has been substantial compliance in good faith with the requirements of paragraph (a). This would seem to override the tests of common law and the Texas Partnership Act for determining whether or not a partnership exists. Although the statutory language appears clear on the matter of the formation of a valid limited partnership, a court might decide that there is no valid limited partnership where a corporate general partner has only insignificant assets. This possibility exists because the underlying policy is that in a limited partnership someone should be subject to unlimited liability. Although there is justification for such an argument, once a limited partnership is formed under the statutory scheme, an attack on its validity would be most successful where fraud or deceit are proved. Regardless of the reason for a court ruling that an organization was not a valid limited partnership, its holding the partners liable as general partners would most likely be conclusive that under state law the organization is a general partnership, especially where there is a finding of associates entering into business for profit. Thompson v. Schmitt, 115 Tex. 53, 274 S.W. 554 (1925); Wells v. McKay Tel.-Cable Co., 239 S.W. 1001, 1006 (Tex. Civ. App. 1922).

Such participation makes one liable as a general partner. **Uniform Limited Partnership Act** § 7.

"(N) No relevant source—the statute, the Commissioners' notes explaining the ULPA, or the cases—gives precise guidelines for determining the nature and quantity of activity which violates the control test." Feld, *The "Control" Test for Limited Partnerships*, 82 H Arv. L. Rev. 1471, 1474 (1969). "Neither the Act nor the decisions under it are very helpful on the critical question of how much review, advisory, management selection, or veto power a limited partner may have without being regarded as taking part in control. The resulting uncertainty is probably the greatest drawback of the limited partnership form." J. CRANE & A. BRONBERG, PARTNERSHIPS 147 (1968).


(b) A limited partner shall not be deemed to take part in the control of the business by virtue of his possessing or exercising a power, specified in the certificate, to vote upon matters affecting the basic structure of the partnership, including the following matters or others of a similar nature:

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<td>(I)</td>
<td>Election or removal of general partners.</td>
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<td>(II)</td>
<td>Termination of the partnership.</td>
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<td>(III)</td>
<td>Amendment of the partnership agreement.</td>
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<td>(IV)</td>
<td>Sale of all or substantially all of the assets of the partnership.</td>
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(c) The statement of powers set forth in subdivision (b) shall not be construed as exclusive or as indicating that any other powers possessed or exercised by a limited partner shall be sufficient to cause such limited partner to be deemed to take part in the control of the business . . . .
the partnership and could be implied from the basic partnership relationship. Since the statute goes on to say that the powers enumerated are not exclusive; it too is of little help in determining how fully a limited partner can participate.

Although the cases commenting on this question are not numerous, there are enough from which to draw some conclusions. Reviewing the cases decided after a majority of states had adopted the ULPA, one finds six that are frequently cited for their useful guidelines. A brief statement of the facts and holdings of these six cases, arranged in order from the least amount of control exercised to the greatest amount of control exercised, indicates that courts are deciding the cases in light of the extent and effect of the limited partner’s actual participation. In Rathke v. Griffith the court was faced with a group that was to act as the “directors” of the partnership, and one of the limited partners was elected to the position of a partnership “director.” Although the limited partner held this office, a great deal of evidence was presented showing that he did not carry out the duties of his office. Based on this lack of actual participation the court found that the limited partner did not exercise any control and was not liable as a general partner. In Granger v. Antoyan a limited partner served as the sales manager of an automobile agency. He signed checks occasionally, but could not hire or fire, buy new cars, or set sales prices or trade-in values. He was held not to be liable as a general partner. In Silvola v. Rowlett a limited partner served as the repair shop foreman and discussed major problems with the general partner. However, since the general partner had exclusive control, the limited partner was not held liable. In Plasteel Products Corp. v. Helman a trustee of a limited partnership interest took part in the hiring of the sales manager and could co-sign checks, but the sales manager could be fired without his consent and others could sign checks without him. Citing Granger, the court held that he was not taking part in control to the extent necessary to be held liable as a general partner. A much cited case in which the limited partners were held liable is Holzman v. De Escamilla. In this case the two limited partners told the general partner which crops to plant on partnership property, and signed the partnership checks. Another case in which limited partners were held liable is Bergeson v. Life Insurance Corp. of America. This case involved a limited partnership which had been formed for the sole purpose of organizing and owning a corporation. The limited partners became directors of the corporation and actively participated in its management. The court found that stock in the corporation had been issued without

The earliest of these cases was decided in 1948. By this time thirty states had adopted the ULPA. See note 19 supra.

48 Cal. 2d 805, 313 P.2d 848 (1957).
571 F.2d 354 (1st Cir. 1978).
the corporation's receiving a just amount of consideration in return, and
held that the limited partners were liable as general partners.

Whether or not a limited partner exercises indirect control merely
through ownership of voting stock, so that he could be held liable as a
general partner, is a very serious concern. In the extreme situation where
the limited partners completely control the corporate general partner, they
could find themselves in trouble due to the rule that is now generally
accepted by the courts that whenever stockholders use their control of a
corporation to achieve injustices, the corporate veil can be pierced and the
stockholders held individually liable. Even in situations which are not
extreme, a finding of enough control to hold limited partners liable as
general partners is conceivable where a partner or partners own enough
stock in the corporate general partner to elect at least one director. It
might be argued that by electing a director the shareholders are indirectly
taking part in the control of the business. As yet, an argument based on
indirect control has not been utilized in any reported cases, but the
rationale is logical.

II. BACKGROUND OF THE TREASURY REGULATIONS

The tax classification of limited partnerships with a corporate general
partner requires careful analysis because the intricacies of the legal rela-
tionships created by state law make it difficult to apply the standards set
out in the Treasury Regulations. Under the Internal Revenue Code: "The
term 'partnership' includes a syndicate, group, pool, joint venture, or
other unincorporated organization . . . which is not, within the meaning
of this title a trust or estate or a corporation. . . . The term 'corporation'
includes associations, joint-stock companies, and insurance companies."4

Difficulty is created by the language of the Code in that the partnership
definition excludes corporations, but the corporation definition does not
exclude partnerships. To clarify the definitions, the Internal Revenue
Service has issued a series of regulations setting out standards for each of
the three classes of business organizations—associations (taxable as corpora-
tions), partnerships, and trusts. The regulation applicable to partnerships
states that an organization qualifying as a limited partnership under state
law may be classified for tax purposes as an association if, after the stan-
dards in the regulation dealing with associations are considered, the limited
partnership more closely resembles a corporation than a partnership.

4Fountainbleau Hotel Corp. v. Crossman, 323 F.2d 937 (5th Cir. 1963). But the corporate
fiction should not be disregarded because of identity of corporation, stockholders, and officers and
the fact of ownership of stock in one corporation by another. Roy Overstreet v. Southern Ry.,
371 F.2d 411 (5th Cir. 1967). To pierce the corporate veil, there must be facts presented to show
that equities justify piercing. In Texas this requires two elements: (1) substantial identity of in-
terests between the individuals and corporation, such that an act of one is an act of the other, and
(2) danger that the corporation will be used or is being used to achieve an inequitable result.


47Internal Revenue Code of 1954, § 7701 (a) (2).

48Id. § 7701 (a) (1).

49Treas. Reg. § 301.7701-2 (1960) (associations); id. § 301.7701-3 (partnerships); and id.
301.7701-4 (trusts).

50Id. § 301.7701-3 (b).
The regulation dealing with associations sets out six corporate characteristics: (1) associates, (2) an objective to carry on business and divide the gains therefrom, (3) continuity of life, (4) centralization of management, (5) liability limited to assets, and (6) free transferability of interests. Since (1) associates, and (2) an objective to carry on a business and divide the gain, are characteristics that are common to both partnerships and corporations, these two characteristics are immaterial in distinguishing between the two. Thus, the classification of a limited partnership with a corporate general partner as a partnership or as a corporation for income tax purposes is a fact question to be decided on the basis of the remaining four characteristics.

The regulations are the result of a long turbulent struggle in the development of the application of the income tax laws to various types of organizations. The rule of using corporate characteristics as the criteria for the classification of an organization was first established by the Supreme Court in the 1935 landmark case of Morrissey v. Commissioner. Faced with the problem of the proper classification of an organization created under a declaration of trust, the Court set out the six characteristics of a corporation and said that if an organization more closely resembled a corporation than another type of business organization, then it should be classified as one and taxed accordingly. This rule became known as the "resemblance test," and regulations embodying the test were promulgated under the Internal Revenue Code of 1939.

When it became apparent to taxpayers during and after World War II that the increasing personal tax rates made taxation as a corporation advantageous in some situations, many professional groups created associations and filed corporate tax returns. The Internal Revenue Service opposed this movement and in 1954 another landmark case, United States v. Kintner, was decided. The Court of Appeals for the Ninth Circuit was faced with the question of the proper classification of a group of doctors who were operating a clinic under "articles of association" which were designed so that under the standards of Morrissey it could be taxed as a corporation. The court held for the taxpayers and affirmed a finding that the association more closely resembled a corporation. The court thereby rejected the Service's argument that an organization should be taxed as a partnership because the state law prohibited a corporation from practicing medicine. Subsequently, in order to make it more difficult for an unincorporated association to meet the standards of corporate resemblance, the Service issued new regulations. These "Kintner Regulations" were issued under the Internal Revenue Code of 1954 and appeared in 1960. In addition to specifically directing the courts to look to state law for the determination

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50 Id. § 101.7701-2(a)(1).
51 Id. § 101.7701-2(a)(2).
52 296 U.S. 344 (1935).
53 Id. at 360.
54 Treas. Reg. 103, §§ 10.3797-1 to -7 (1939); id. 111, §§ 29.3797-1 to -7 (1943); id. 118, §§ 39.3797-1 to -7 (1953).
55 216 F.2d 418 (9th Cir. 1954).
of whether or not a particular corporate characteristic existed, a regulation required that "more corporate characteristics than noncorporate characteristics" be present before an organization could be classified as an association. 

After the issuance of the "Kintner Regulations," many states changed their corporate laws to enable professional organizations to incorporate. Desiring to allow their professionals the benefit of favorable tax treatment, state legislatures reasoned that the regulations applied only to unincorporated organizations. To counter this action by state legislatures, the Service amended the "Kintner Regulations" in 1965 specifically to cover incorporated professional organizations. However, the Service has failed in its attempt to enforce the amended regulations; three circuit courts have held that the amendment applying to incorporated organizations is invalid. In August of 1969, the Service conceded that organizations of professionals organized under state professional corporation statutes would be treated as corporations. Since neither the court decisions nor the change in the Service's position invalidated the unamended "Kintner Regulations," they must logically be considered as the criteria for classifying a limited partnership with a corporate general partner, and these regulations set forth each of the four distinguishing corporate characteristics in detail.

III. CORPORATE CHARACTERISTICS

Continuity of Life. The first of the four corporate characteristics, continuity of life, is explained by a regulation as follows:

An organization has continuity of life if the death, insanity, bankruptcy, retirement, resignation, or expulsion of any member will not cause a dissolution. . . . If the retirement, death, or insanity of a general partner of a limited partnership causes a dissolution of the partnership, unless the remaining general partners agree to continue the partnership or unless all remaining members agree to continue the partnership, continuity of life does not exist.

The regulation adds that if a member has the power under local law to dissolve the partnership, there is no continuity of life, and accordingly, a limited partnership subject to a statute based upon or similar to the Uniform Limited Partnership Act lacks this corporate characteristic. The ULPA provision concerning the power to dissolve states that "the retirement, death or insanity of a general partner dissolves the partnership, unless

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87 Treas. Reg. § 301.7701-1(c) (1960).
88 Id. § 301.7701-2(a) (3).
89 Id. § 301.7701-1(c) (1961) was amended to cover these groups; id. § 301.7701-2(h) was added to make it almost impossible for them to qualify as associations; and id. § 301.7701-2(g), an illustration of an association that had been approved, was deleted from the list of examples. T.D. 6797, 1965-1 CUM. BULL. 553.
90 Kurzner v. United States, 413 F.2d 97 (5th Cir. 1969); O'Neill v. United States, 410 F.2d 888 (6th Cir. 1969); United States v. Empey, 406 F.2d 157 (10th Cir. 1969).
91 Treas. Reg. § 301.7701-2(h) (1965).
93 Treas. Reg. § 301.7701-2(b) (1) (1960).
94 Id. § 301.7701-2(b) (3).
the business is continued by the remaining general partners . . . .

In a limited partnership with a corporation as the sole general partner, there are no remaining general partners to continue the business if the corporation for some reason becomes defunct. Even where the limited partners control the corporation, making it unlikely that the corporation will withdraw, it could still become bankrupt and dissolution would result. As a result, it seems that a limited partnership with a corporate general partner organized in a ULPA state could not comply with the regulation's standard for the corporate characteristic of continuity of life.

Centralized Management. The second corporate characteristic, centralized management, is defined by a regulation as "concentration of continuing exclusive authority to make independent business decisions on behalf of the organization which do not require ratification by members of such organization." The regulation states that if subject to a statute corresponding to the ULPA, the limited partnership does not generally have centralized management; but the regulation further states that the partnership does have centralized management if substantially all the interests in the partnership are owned by the limited partners. This conclusion is based on the reasoning that while centralized management is a characteristic of a limited partnership, the type of management is a different type of centralized management from that of a corporation. Centralized management in the corporate sense means management in a representative capacity, i.e., directors manage a corporation, but as representatives of the stockholders. In the limited partnership sense, centralized management means that the general partner has the exclusive management power, subject only to the fiduciary duty he owes to the other partners. He should primarily be acting in his own behalf. The regulation recognizes that if the limited partners own substantially all the interests of the partnership, then the general partner can only be acting on their behalf. If the corporate general partner is controlled by the limited partner, the corporation would be acting in a representative capacity and the partnership would possess this corporate management characteristic. Factors which might be considered in evaluating the interest of the corporate general partner in a limited partnership are (1) its capital contribution in relation to that of the limited partners, (2) its percentage of partnership profits or income, (3) its services performed, and (4) the limited partners' control of the corporate general

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56 Uniform Limited Partnership Act § 20.
57 11 U.S.C. § 11 (1965). When all general partners are adjudged bankrupt, so is the partnership.
59 The term "interests" is not defined by the Regulations.
61 Uniform Limited Partnership Act § 2. A general partner has all the rights and powers of a partner in a partnership without limited partners except that without written consent or ratification by all the limited partners, he may not: (a) contravene the certificate, (b) make it impossible to carry on the business, (c) confess to a judgment against the partnership, (d) possess or assign partnership property other than for a partnership purpose, (e) admit another general partner, (f) admit a limited partner, unless given the right by the certificate, and (g) continue the business on the death, retirement or insanity of another general partner, unless given the power to do so by the certificate.
62 Uniform Partnership Act §§ 18-23.
partner. Therefore, in order for a limited partnership with a corporate
general partner to avoid having corporate centralized management under
the regulation, the limited partners should not own substantially all the
interests of the partnership and should not control the corporation. Providing
such independence for the corporate general partner also strengthens
the classification of the organization as a partnership under state law.

Limited Liability. A regulation defines the third corporate characteristic,
limited liability, as the existence of no member who is personally liable for
claims against the organization under local law.\footnote{Treas. Reg. § 301.7701-2(d)(1) (1960).} Further, the regulation
defines personal liability as a creditor’s ability to seek satisfaction from the
members as individuals when the organization’s assets are insufficient to
satisfy his claim. The regulation adds that in the case of a limited part-
nership subject to a statute corresponding to the ULPA, personal liability
exists as to each general partner, except in partnerships in which the gen-
eral partner has no substantial assets other than his interest in the part-
nership.\footnote{Id. § 301.7701-2(d)(2).} It then specifically discusses a corporation as the general partner by
stating that personal liability exists if the corporation has substantial assets
other than its interest in the partnership which could be reached by a
partnership creditor.\footnote{Id.} Thus, the regulation recognizes the practical
situation that may very well exist when a corporation is the general partner.
Since only the general partner has liability beyond his interest in the part-
nership under the ULPA,\footnote{Uniform Limited Partnership Act §§ 9-10.}
if the corporate general partner has no other
assets than its partnership interest, creditors would have to look only to
assets of the partnership. This is precisely the situation a creditor would
face in dealing with a corporation, so the corporate characteristic would
be present. The appropriate manner by which a limited partnership with a
corporate general partner would avoid the corporate characteristic of
limited liability under the regulation standard is for the corporation to
have substantial assets\footnote{According to the unofficial position of the Service, a corporate general partner should have
a net worth equal to the greater of $250,000 or 10\% of the partnership capitalization. See note 110 infra.} other than its interest in the partnership.

Another consideration is whether or not any limited partner is liable as
a general partner. Under the ULPA, possible liability could result in several
situations: a limited partner’s name is part of the firm name;\footnote{Uniform Limited Partnership Act § 5(2).} a limited
partner holds himself out to be a general partner;\footnote{Id. § 16.} the partnership is
defectively organized and upon discovering it, the limited partner does
not renounce his interest in the profits;\footnote{Id. § 11.} and as discussed earlier, a limited
partner takes part in the control of the business.\footnote{Id. § 7. See text following note 45 infra. Another situation which gives rise to liability
greater than one’s contribution is where a limited partner is compelled to guarantee partnership
loans, but the amount of liability would be definite, not unlimited.} If any of these occurred,
the limited partner would have personal liability.\textsuperscript{81} The imposition of unlimited liability is, under the Regulations, a partnership, not a corporate characteristic.\textsuperscript{82} However, the imposition of liability on limited partners because of indirect control through stock ownership would also have the effect of creating the corporate type of centralized management, because where the limited partners control a director he would be acting in a representative capacity for them.\textsuperscript{83} The net result of such a case, where limited partners were held liable as general partners because of the exercise of indirect control, would seem to be that the organization would gain the corporate characteristic of centralized management, but lose the corporate characteristic of limited liability. In such a case, because a limited partnership under the ULP\textsuperscript{A} cannot have the corporate continuity of life in the Service's view,\textsuperscript{84} it would seem that the partnership should still not be classified as an association as it would not have three corporate characteristics.\textsuperscript{85}

Free Transferability. A regulation defines the fourth corporate characteristic, free transferability of interests, as: "Each of its members or those members owning substantially all of the interests in the organization have the power, without the consent of other members, to substitute for themselves in the same organization a person who is not a member of the organization . . . [and] to confer upon his substitute all the attributes of his interest in the organization."\textsuperscript{86} The regulation also recognizes as a modified form of free transferability, an agreement requiring a member to first offer to sell the interest to the other members at its fair market value before transferring to someone who is not a member.\textsuperscript{87} However, the regulation directs that such rights of first refusal be given less significance than the unmodified forms of free transferability.\textsuperscript{88} The regulation standard is such that under the ULP\textsuperscript{A} a limited partnership normally would not have this corporate characteristic. If the corporate general partner owns substantially all the interest in the partnership, this standard would not be met. The ULP\textsuperscript{A} states that a limited partner's interest is assignable, but also states that the assignee is not admitted to all the rights of the transferor unless all the members consent or the certificate gives the assignor the power to confer all his rights.\textsuperscript{89} Thus, where the limited partners own substantially all the partnership interests, a specific prohibition against transfer is unnecessary. If the certificate merely follows this provision of the ULP\textsuperscript{A} requiring consent of all the members to allow an assignee to

\textsuperscript{81} Treas. Reg. § 301.7701-2(d)(1) (1960): "Personal liability means that a creditor of an organization may seek personal satisfaction from a member of the organization to the extent that the assets of such organization are insufficient to satisfy the creditor's claim."

\textsuperscript{82} Treas. Reg. § 301.7701-2(d)(1) (1960).

\textsuperscript{83} See text accompanying notes 67-71 supra.

\textsuperscript{84} See notes 63-66 supra, and accompanying text.

\textsuperscript{85} See note 58 supra.

\textsuperscript{86} Treas. Reg. § 301.7701-2(e)(1) (1960).

\textsuperscript{87} Id. § 301.7701-2(e)(2).

\textsuperscript{88} Id.

\textsuperscript{89} Uniform Limited Partnership Act § 19(4).
become a substituted partner, the partnership would not meet the standard for this corporate characteristic.

According to the regulations, an organization must have "more corporate characteristics than noncorporate characteristics" to be classified as an association. The reason for this particular wording is that, as pointed out previously, the regulations were designed to make it difficult for partnerships to achieve corporate tax treatment. The regulation states that if a limited partnership has centralized management and free transferability of interests but lacks continuity of life and limited liability, absent any other characteristics that are significant in determining classification, it will not be classified as an association. Thus, under these regulations, as long as a limited partnership possesses less than three of the four corporate characteristics, in the past it has been classified as a partnership.

Under id. § 19(2), a substituted partner is a person admitted to all the rights of a limited partner.

There is no indication of what is meant by this clause. The trend since Morrissey v. Commissioner, 296 U.S. 344 (1935), has been to concentrate on the four, excluding (1) associates, and (2) an objective to carry on business and divide the gains, since both of these are common to partnerships and corporations. For examples of what might be considered other characteristics, see notes 100-02 and 106 infra, and accompanying text.

Example (1)

Facts Applicable to Both

Three individuals who will be the general partners form an organization which qualifies as a limited partnership under state law. Its purpose is to acquire and operate commercial and investment property for profit. The limited partners contribute a total of $5,000,000.

Life

Life is 20 years, but the death, insanity, or retirement of a general partner prior to the end of 20 years will dissolve the organization.

Management

The general partners have exclusive authority to manage the affairs of the organization but can act only upon the unanimous consent of all of them.

Liability

Each of the general partners invests $100,000 and is personally capable of assuming a substantial part of the obligations to be incurred by the organization.

Transferability of Interest

A limited partner (there are 30 with a minimum contribution of $100,000) may assign his right to receive a share of the profits and a return of his contribution, but his assignee does not become a substituted partner except with the unanimous consent of the general partners.

Example (2)

Facts Applicable to Both

Life is 40 years, unless a general partner dies, becomes insane, or retires, but in the event of one of these, the remaining general partners may continue the business for the balance of the 40 years.

Life

Life is 40 years, unless a general partner dies, becomes insane, or retires, but in the event of one of these, the remaining general partners may continue the business for the balance of the 40 years.

Management

The general partners have exclusive control over management of the business.

Liability

Each of the general partners invests $50,000 and has means to satisfy the business obligations of the organization to a substantial extent.

Transferability of Interest

The limited partners' interests (there are 900 limited partners with a maximum contribution of $10,000) are freely transferable.

The regulation concludes that both of the examples will be classified as partnerships for all purposes of the Internal Revenue Code. It states that in example (1) the limited partnership has the corporate characteristic of centralized management since substantially all the interests in the organization are owned by the limited partners; it does not have the characteristics of continuity of life, limited liability, and free transferability of interest. The regulation states that the limited partner-
Application of the Regulations. The leading case discussing the application of the standards to an actual fact situation, and a case to which the Internal Revenue Service has acquiesced, is Glensder Textile Co. v. Commissioner.55 Glensder Textile Co. was a limited partnership established in 1936 under the New York Uniform Limited Partnership Act56 by the four general partners of an old ordinary partnership, redistributing the $300,000 net worth between themselves as general partners and their wives and children as limited partners. The general partners' contributions totalled $125,000 and they were to receive a proportionate 5/12ths of the profits. The other $175,000 net worth belonged to the limited partners who were to receive a proportionate 7/12ths of the profits. There was no question as to the validity of the ownership of the various interests. The Commissioner contended that the limited partnership more closely resembled a corporation. Based on the New York statutes57 and the partnership certificate, the court found that the organization did not more closely resemble a corporation because it lacked the necessary corporate characteristics. The court found that although the certificate gave the remaining general partners the right to continue the business on the death, retirement, or insanity of one or more of them, it was not "analogous to the chartered life of a corporation which continues regardless of the death or resignation of its directors or stockholders."58 The continuity was contingent, giving the partners the right to continue, but not insuring that they would continue. If they did decide to continue, there was, in effect, a new partnership. This does not comply with the standard set out in the regulation. The court also found that although centralized control by the general partners existed, it was not the type which made them analogous to directors. They acted in their own interests, which constituted 5/12ths of the partnership, and they could not be removed by the limited partners.

Further, the court found that limited liability did not exist in the corporate sense. The court stated that the limited liability of the limited partner should not be the final criterion. It is important that the persons in control of the partnership activities were the general partners who, under the statutes, had unlimited liability. The court also noted that should a limited partner enter into business activity, he would become liable as a general partner. In discussing the transferability of interests, the court pointed out that the limited partners, under the certificate, could assign their interests and had the power to confer upon the assignee the rights of a substituted limited partner if they chose to do so. However, the court noted that there were no mechanics provided for free transferability

ship in example (2) has the corporate characteristics of centralized management since the three general partners exercise exclusive control over the management of the business and substantially all of the interests in the organization are owned by the limited partners. Also, the limited partnership has free transferability of interests since substantially all of the interests in the organization are represented by transferable certificates owned by limited partners. It does not have the corporate characteristics of continuity of life and limited liability.

55 46 B.T.A. 176 (1942), acquiesced in 1942-1 CUM. BULL. S.
56 N.Y. PARTNERSHIP LAW §§ 90-119 (McKinney 1948).
57 Id.
58 46 B.T.A. at 185.
through certificates representing shares. The court also noted that if a limited partner merely assigned his interest without substitution, the assignee's position "would bear no resemblance to a corporate stockholder's status." Finally, the court pointed out that the general partner's interest was not transferable any more than was one in a general partnership.

The court went on to consider other characteristics of the partnership which could have a bearing on its classification. In further discussing the classification of the organization, the court stated that it seemed immaterial that the limited partnership could hold the title in real estate in the partnership name because under another statute partnership property is held by the partners as tenants in partnership; therefore, whether the title is held in the name of a partner or the partnership, the equitable title is in the name of the several partners. Further, the court pointed out that a limited partnership may not sue in its own name; the general partners are the proper party plaintiffs.

Another illustrative case involving the classification of limited partnerships is Riggs v. Commissioner. In that case the tax court was presented a controversy in which the taxpayer dissolved a corporation owned by himself and his son and created a limited partnership in 1938. The Commissioner contended that the partnership possessed each of the corporate characteristics and should be classified as an association. He emphasized his contention that the limited partnership had continuity of life and centralization of management, which characteristics were all that the regulations existing prior to Kintner required. The court found that the partnership did not have continuity of life in the corporate sense. Citing Glensker, the court stated that the partnership agreement providing that if any partner ceased to be associated with the partnership the business would continue under the management of the remaining partner or partners merely provided for the nonliquidation, which is not a rarity in partnership arrangements. The court found that the certificate giving exclusive management powers to the taxpayer and his son and giving the taxpayer the controlling vote in case of disagreement did not create centralized management. The court pointed out that "[T]he power is not so rare a provision in partnership agreements as to require our holding that this enterprise was more than an ordinary partnership."

The court simply rejected the Commissioner's argument that the sharing of profits and losses in a certain percentage is not an attempt to limit liability as it only affects the partners, not third persons not party to the agreement. The court also found that since there were no certificates of

99 Id. at 186.
100 N.Y. PARTNERSHIP LAW § 12(1) (McKinney 1948).
101 Id. § 51(1).
102 Id. § 115.
103 6 T.C. 889 (1946).
104 A certificate was filed on Jan. 6, 1944, pursuant to an Arkansas statute adopted in 1943.
105 6 T.C. at 897.
ownership or beneficial interests issued and that since new partners could enter the firm only with the consent of all the other partners, free transferability of interest did not exist. The court noted that the books were prepared and kept in accordance with recognized rules of partnership accounting and that they contained none of the accounts peculiar to corporations. It also stated that customers, banks, and other business connections regarded the organization as a partnership and specifically pointed out that signature cards used when the bank account was opened were those used for partnerships and individuals, and the bank did not require a corporate resolution authorizing the withdrawal of funds. The court summed up by saying that, if anything, the taxpayer's case is stronger than that of George Bros. & Co., a case involving a general partnership which the Internal Revenue Service tried, but failed, to have classified as an association.

IV. INTERNAL REVENUE SERVICE POSITION

The position that the Internal Revenue Service will take with regard to the classification of a limited partnership with a corporate general partner is uncertain. There are no litigated cases involving this type of organization in which any opinion is expressed, and the Service has not published an official policy. Until now the Service's efforts have been primarily concerned with challenging associations' and professional corporations' attempts at attaining corporate taxation. Having lost, they may now feel free to reverse their position in applying the regulations to limited partnerships with a sole corporate general partner.

The author understands that the Service's current position is as follows. Officers and directors of the corporate general partner can be limited partners, but the limited partners cannot own in excess of twenty per cent of the stock of the corporate general partner, and no packages of stock in the corporate general partner and limited partnership interests, or warrants to purchase stock of the corporate general partner and limited partnership interests, can be offered. In addition, the minimum capitalization of the corporate general partner after the underwriting has been completed and throughout the existence of the limited partnership should be fifteen per cent of the total capital of the limited partnership on the first $1,666,667, at least $250,000 if the total capital is between $1,666,667 and $2,500,000, and ten per cent of the total capital if the total capital exceeds $2,500,000. The percentage is computed on the fair market value of the corporation's assets including its interest in the limited partnership, and the net worth requirement is non-cumulative where the corporate general partner is the general partner of more than one venture.

106 Id.
107 Id.
Tax Management has previously published its understanding that the Internal Revenue Service would rule favorably on the qualification of the limited partnership as a "partnership" if the limited partners did not own, directly or indirectly, more than twenty per cent of the outstanding stock of the corporate general partner or a corporation which is affiliated with the corporate general partner within the definition of "affiliated group" in section 1504 of the Code. Tax Management has also suggested that, in addition, the Service would rule that a limited partner having a corporate general partner would not be an association taxable as a corporation if the corporate general partner had a net worth, measured by book value, at least equal to $250,000, or ten per cent of the capitalization of the limited partnership, whichever were greater.

The uncertainty of the Service's attitude, due to its not publishing a ruling, is creating serious problems. A preliminary prospectus for the shares of stock in a corporation which plans to form a series of limited partnerships to conduct oil and gas exploration stated: "Because of present federal income tax policies, no limited partner in the Fund or any future limited partnership formed for similar purposes . . . may own, directly or indirectly, any shares of the common stock of the Company, including any of the shares . . . offered hereby." Further, the prospectus explained that the purpose of the restriction is to assure all limited partners that there will be no common ownership which will adversely affect the partnership status of the organization and, as a result, the pass-through of deductions.

The Service's position is difficult to understand. The rules for classifying organizations are well established. It seems as though the only thing that identity of limited partners and stockholders would do is establish indirect control which would not in itself be determinative of classification. The amount of a corporation's net worth only goes to the "substantial interest" of the general partner. Whether or not a corporate general partner has a substantial interest does affect the characteristics of limited liability and centralized management, but according to regulations the general partner's lacking a substantial interest would prohibit the corporate characteristic of limited liability but would add the corporate characteristic of centralized management. This situation, as with the limited partners, would not in itself be determinative under the long-standing Morrissey doctrine. The Internal Revenue Service appears to be trying to discourage the use of the limited partnership with a corporate general partner by withholding a ruling that it will recognize them as partnerships for tax purposes.

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108 INT. REV. CODE of 1954, § 1504 defines "affiliated group" as one or more chains of includable corporations connected to a common parent corporation through stock ownership. The stock ownership of the various corporations must be 80% of all classes of non-voting stock.
112 Id.
113 Indirect control would normally only have an effect on limited liability and the type of centralized management which the partnership possesses. See text following note 83 supra.
114 Treas. Reg. § 301.7701-2(d)(2) (1960); see notes 72-74 supra, and accompanying text.
115 Treas. Reg. § 301.7701-2(c)(4) (1960); see notes 67-71 supra, and accompanying text.
Even though the Service does withhold ruling, it may not be successful in litigation over the classification of those limited partnerships formed under the ULPA with some attention given the regulations in wording the partnership certificate. The reason is that regulations require that a partnership possess three of the four corporate characteristics before it is to be classified as an association.\footnote{Treasury Reg. § 301.7701-2(a)(3) (1960).} Even if the Service, because of its loss in attacking professional corporations, attempts to go back to the pre-Kintner regulations, which stressed continuity of life and centralized management,\footnote{Treas. Reg. 118, § 39.3797-4 (1953), states that if an organization is not interrupted by the death of a member or a change of ownership, and if management is centralized, "such organization is an association, taxable as a corporation."} it would still have difficulty where the taxpayer words his agreement and certificate carefully.\footnote{Glensler Textile Co., 46 B.T.A. 176 (1942), and other cases decided prior to the 1954 Code were decided in favor of the taxpayer. See notes 95-107 supra, and accompanying text.}

V. Conclusion

Limited partnerships with a corporate general partner are useful as vehicles for raising the large amounts of capital needed for types of enterprises such as oil and gas exploration and real estate development. They offer an alternative to conducting the business in the corporate form while still giving investors the protection of limited liability. There are practical differences between a limited partnership and a corporation. Limited partners do not participate in management even as much as shareholders do in electing directors, and limited partnerships are usually less flexible because of the narrower scope of purposes in a limited partnership certificate and the frequent need to amend it, contrasted to the wide range of powers enjoyed by a corporation under its charter. Other differences are more technical than practical. The corporate characteristic of free transferability of interests can be attained or avoided by wording the partnership certificate accordingly. The provisions of the ULPA which technically deny partnerships continuity of life and limited liability can be circumvented, for all practical purposes, by giving the remaining partners the power to continue after a technical dissolution and by choosing a general partner with limited assets. Nevertheless, the distinctions and standards set out in the Regulations are such that it would indeed be difficult for a limited partnership organized under the ULPA or similar statute to be correctly classified as an association for tax purposes. The fact that the Regulations were designed to prevent partnerships from being classified as associations, will make it difficult for the Internal Revenue Service to apply them in a manner so as to now have partnerships classified as associations. Neither will the Service be able arbitrarily to create new standards under which partnerships would be classified as associations, as evidenced by the litigation concerning professional corporations.\footnote{See notes 60-62 supra, and accompanying text.}

In order to avoid a possible round of litigation similar to that concerning professional corporations, some definite guidelines should be developed...
after a thorough study has been made of the limited partnership with a corporate general partner—its place in the economy, weighing the economic benefits provided by it against the loss of revenues due to the tax benefits that may be derived from it. Limited partnerships, including those with a corporate general partner, do offer economic as well as tax benefits. Many expensive business undertakings would not be possible without the large amount of money that private individuals are willing to invest, but individuals with a great deal of money are acutely concerned with income taxation and will be more disposed to invest in business organizations which have favorable tax treatment. Taxation has long been used by the government to accomplish other things besides raising revenues. It is evident from the Tax Reform Act of 1969 that the government is trying to influence the area in which investments are made because it lowered the oil and gas depletion allowance percentage and reduced the depreciation available on everything except for residential rental property, which can still be depreciated by the double declining balance method.¹⁰⁰

When interest rates drop and increasing amounts of money are made available for investments,¹¹¹ much of it could be directed into limited partnerships with a corporate general partner. Hopefully, more definite guidelines will be set forth by the Internal Revenue Service for investors and developers desiring to make use of these organizations. If the Service does not act, Congress should.

¹⁰⁰ See note 9 supra.
¹¹¹ At present, mortgage companies are not making a great many real estate loans. The loans which are made are usually with a rate of interest between 9 1/2% and 10% plus participation by the mortgage company. Interview with John Tatum of M.P. Crum Co., a mortgage banker in Dallas, Texas, Apr. 6, 1970.