

## **RENKEMEYER COMPOUNDS THE CONFUSION IN CHARACTERIZING LIMITED AND GENERAL PARTNERS—PART 2**

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*The Tax Court reached the correct result in finding that the attorney-partners in a law firm operating as a limited liability partnership had net earnings from self-employment, and were therefore liable for self-employment tax. But the court's approach to the issue of who is a limited partner has already had a widespread ripple effect that has focused practitioner concern on the differences and similarities between the various types of pass-through limited liability entities.*

As discussed in Part 1 of this article,<sup>1</sup> an ongoing question is who or what, for tax purposes, is a “limited partner” or “general partner” of an unincorporated business entity taxable as a partnership.<sup>2</sup> The answer can result in substantial adverse—or favorable—tax consequences for the members of the tax partnership, under the numerous Code and regulatory provisions that use those terms. For example:

- By operation of Section 1402, an individual member of an unincorporated business entity who already has paid the maximum OASDI portion of the self-employment (SE) tax with respect to other income must pay the unlimited 2.9% HI tax component if she is classified as a “general partner.” Alternatively, a member who is classified as a “limited partner” may avoid the SE tax on her allocable share of partnership income, but cannot make contributions to a qualified retirement plan with respect to her distributive share of partnership income.
- By operation of Section 469, a tax partner classified as a “limited partner” may not be able to meet the (restricted) material participation tests under Temp. Reg. 1.469-5T, for purposes of the passive activity rules, whereas classification as a “general partner” would permit the tax partner to satisfy additional, alternative tests not otherwise available.
- A tax partnership may be able to deduct payments (in the year paid) under Section 736(b)(3) to withdrawn or retired members who were deemed “general partners” for purposes of that section, while payments to those members not classified as “general partners” will not be currently deductible.

There is surprisingly scant guidance (in the form of statutes, Regulations and other administrative guidance, and case law) addressing this topic. The initial focus was on the tax distinctions between general and limited partners in a limited partnership organized and operated under state law, and it expanded to consider whether the members of other types of state law unincorporated limited liability entities, e.g., LLCs, LLPs, and LLLPs (collectively, along with state law limited partnerships, “limited liability entities” or “LLEs”) could be shoehorned into either “limited partner” or “general partner” status for tax purposes.

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In Part 1 of this article we described the nearly century-long state law evolution of LLEs.<sup>3</sup> We also discussed the changes in members' limited liability and level of permissible activity or participation allowable under state law for each form of LLE.<sup>4</sup>

We next identified definitional deficiencies and uncertainties under the tax law in characterizing members of LLEs. We explored nearly 20 different ways to define "general partner" and "limited partner" for tax purposes.<sup>5</sup> We observed that Treasury, the IRS and the courts have not been consistent in their approaches. We attempted to identify the merits and weaknesses of each alternative, in our quest to find the best way to define these terms.

We next shifted our focus in Part 1 to how "limited partner" and "general partner" are defined in those Code provisions where either or both of the terms arise most frequently in practice. There is limited guidance (i.e., final or Proposed Regulations, Rulings, and case law) as to the members' tax status provided under some of these provisions. This leads us to question whether a comprehensive or a section-by-section approach would be the preferred solution.

Part 1 of this article concluded by analyzing the tax law classification of members of LLEs by topic, i.e., the characterization of members of state law limited partnerships, LLLPs, LLCs, and LLPs, respectively, as "limited" or "general" partners for tax purposes.

Here in Part 2 we focus on the Tax Court's curious opinion last year in *Renkemeyer, Campbell & Weaver, LLP*, 136 TC 137 (2011). There, the court ruled in a case of first impression that members of a law firm operating as an LLP were not "limited partners" for purposes of avoiding self-employment (SE) tax under Section 1402(a)(13) on their respective allocable shares of the partnership's income.<sup>6</sup> The method of analysis used in *Renkemeyer* may foreshadow how the Tax Court (and other courts) will characterize members of other unincorporated business entities for purposes of the dozen Code and 70-plus Regulations provisions that provide differing tax consequences for "limited partners" and "general partners."

If the Tax Court's methodology is broadly applied to situations other than under Section 1402(a)(13), those members may be characterized as "limited partners" for some tax purposes and "general partners" for others—a logically inconsistent, sometimes unpredictable, but oftentimes appropriate result, in our view. Moreover, by signaling that LLP and LLC members are not automatically "*not* limited partners," *Renkemeyer* is inconsistent with the analytical method used by the Tax Court (and some other courts) in cases under Section 469.

As will be discussed herein, *Renkemeyer* sheds some light on the Tax Court's characterization for tax purposes of members of LLPs and other unincorporated entities while simultaneously leaving many questions unanswered, raising additional questions, and creating more than a little confusion. (The AICPA and others have called for regulatory guidance in light of the uncertainty that *Renkemeyer* has added to the treatment of limited partners and LLC members.<sup>7</sup>) *Renkemeyer* also has reignited interest in a topic that percolated politically in the late 1990s—the SE tax liability of state law limited partners who provide services to their partnerships.

This Part 2 also analyzes the characterization of members of unincorporated business entities as "limited partners" and "general partners" in light of *Renkemeyer* and other recent judicial developments. We first will analyze *Renkemeyer* with respect to its classification of LLP members for purposes of Section 1402(a)(13). After identifying questions left unanswered by the court's decision, we will then focus on whether *Renkemeyer* provides guidance for purposes of the classification of members of unincorporated entities other than LLPs under Section 1402(a)(13). Finally, and perhaps most important, we will discuss whether *Renkemeyer* signals how the Tax Court (and perhaps other courts) will classify members of LLEs as limited or general partners for purposes of other operative Code provisions.

The analysis herein also will cover recently Proposed Regulations under Sections 469 and 892 that define “limited partners” in a fashion that may be extended to certain operative Code provisions currently lacking such guidance. Indeed, these new Proposed Regulations may signal that Treasury and the IRS view *Renkemeyer* as justification for abandoning reliance on the state law characterization of members of tax partnerships as being “limited partners” or “general partners” for certain purposes under the Code.

## **RENKEMEYER**

Renkemeyer, Campbell & Weaver, LLP was a Kansas limited liability partnership whose principal place of business was Kansas when the petition was filed. The law firm was organized in 2000 and its practice emphasized federal tax law. During the 2004 tax year the partners were Troy Renkemeyer, Todd Campbell, and Tracy Weaver, all lawyers, and RCGW Investment Management, Inc. (RCGW), a Kansas corporation. In the 2005 tax year the law firm’s partners were Messrs. Renkemeyer, Campbell, and Weaver.

During 2004, the LLP’s partnership agreement was amended to provide for two classes of ownership interests: “General Managing Partner Partnership Units” (general managing partner interests) and “Investing Partnership Units” (investing partner interests). The general managing partner interests provided its holders with full authority to act on behalf of the partnership. Pursuant to the amended partnership agreement, each partner was required to contribute \$10 for his general managing partner interest and \$100 for his investing partner interest. The interests were issued proportionately to the three partners: Renkemeyer, Campbell, and Weaver each received a 1% general managing partner interest and a 32% investing partner interest.<sup>8</sup>

Although the law firm reported business revenues from its law practice on the firm’s Forms 1065 for the 2004 and 2005 tax years, no portion of those revenues was included on the law firm’s tax returns as net earnings from self-employment (NEFSE).

The *Renkemeyer* case involved two issues:

- (1) Whether the partners’ distributive share of the law firm LLP’s net business income for tax year 2004 should be reallocated under Section 704, as IRS contended. The court sustained the Service’s reallocation. (As the analysis does not involve characterization of the partners’ interests as limited or general partners, it will not be discussed further herein.)
- (2) Whether the attorney-partners’ distributive shares of the law firm’s business income for the 2004 and 2005 tax years were subject to SE tax. The court’s decision turned on whether the attorney-partners were “limited partners” under Section 1402(a)(13) ; it held they were not.

The Tax Court first analyzed the Code provisions relevant to partners’ SE taxes. Section 1401(a) imposes a tax on the SE income of every individual for a tax year (“the SE tax”). SE income in general is defined as “the net earnings from self-employment derived by an individual ... during any taxable year.”

Section 1402(a) defines NEFSE as “the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in Section 702(a)(8) from any trade or business carried on by a partnership of which he is a member....”

Section 702(a)(8) provides that in determining his income tax, each partner takes into account separately his distributive share of the partnership’s taxable income or loss, exclusive of items requiring separate computation under other paragraphs of Section 702(a). Therefore, in general, a partner must include his distributive share of partnership income in calculating his NEFSE. Fees for services, like those generated by a law partnership, are part of the partners’ distributive shares under Section 702(a)(8). Consequently, such fees are generally included in calculating NEFSE, unless an exclusion applies.

Section 1402(a) provides several exclusions from the SE tax general rule. In particular, current Section 1402(a)(13) provides that “there shall be excluded the distributive share of any item of income or loss of a *limited partner*, as such, other than guaranteed payments described in Section 707(c) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services....” (Emphasis added.)

### **The Taxpayer’s Position**

The partners contended their interests in the law firm (organized as a Kansas LLP) each should be considered a limited partner’s interest in a limited partnership for purposes of Section 1402(a)(13). They claimed their respective interests in the law firm shared the characteristics of a limited partner in a limited partnership because (1) their interests were designated as limited partnership interests in the law firm’s organizational documents,<sup>9</sup> and (2) their interests in the law firm enjoyed limited liability pursuant to Kansas law. Hence, they argued their distributive shares of the law firm’s business income qualified for the Section 1402(a)(13) exception.

As discussed in the taxpayer’s brief, the attorneys exercised management powers and provided management services pursuant to their rights as general managing partners, not as investing partners, the latter having no such right to manage. The taxpayer contended that Section 1402(a)(13) could be applied to characterize each general managing partner interest as a 1% “general partner” interest and each investing partner interest as a 32% “limited partner” interest. If the court were to conclude that each of the partners held both a general and a limited partner interest, the taxpayer contended that Prop. Reg. 1.1402(a)-2(h)(3) would shield all of the LLP’s income from SE tax.

Although the taxpayer argued that each partner’s entire 33% interest should not be characterized for tax purposes as a “general partner” interest, it provided a fallback position. That is, if each attorney’s participation in management was a material factor in the analysis, then the investing partner interests should be deemed to be an interest of a “limited partner” because those interests did not carry the ability to participate in management. (It would presumably follow that almost all, i.e., 97% (which is 32%/33%), of each partner’s allocable share of the LLP’s taxable income would thereby be exempt from SE taxes under Section 1402(a)(13).)

### **The Service’s Position**

The IRS determined that the three individual partners’ distributive shares of the law firm’s net business income were subject to SE tax.

The opinion does not state that the Service concluded the partners were “general partners” for purposes of Section 1402(a)(13). Indeed, the opinion makes no express reference as to what theory or theories the IRS posed to the court in favor of subjecting the attorneys to SE tax. Based solely on the opinion, one might speculate that since the taxpayer bore the burden of proof with respect to this issue, the Service’s position need not be justified unless the taxpayer overcome its burden of proof—which it failed to accomplish in *Renkemeyer*.

The Service’s brief (not cited or discussed in the opinion) makes it clear that the IRS would apply the State Law Characterization Approach<sup>10</sup> to subject all the LLP’s members to SE tax. The IRS observed that the partnership itself is organized and operated as an LLP; an LLP is a general partnership (not a limited partnership) under Kansas partnership law, and under that law there are no limited partners in an LLP. Thus, each attorney received his share of ordinary income from the law partnership as a general partner. Therefore, the attorneys were not limited partners eligible for the Section 1402(a)(13) exclusion from SE tax.<sup>11</sup>

The Service's brief belittles the taxpayer's argument that each partner was primarily a passive investor in the partnership because of bifurcation that allegedly resulted from the investment partner interests. The IRS contended that the attempt to use labels to create a bifurcation of interests of practicing attorneys in a Kansas LLP (with each "general managing partner" simultaneously being an "investing partner") was "little more than a sham." The taxpayer arguably failed to show that the two supposedly separate classes of partnership interests were valid for state law or relevant for federal tax law. Moreover, the introduction of the class of "investing partner" did not have any substance and did not result in a bifurcation of the partners' interests in the LLP. Finally, the IRS contended that even if the court were to conclude that each of the LLP's partners held both a general and a limited partner interest, the taxpayer's assertion that Prop. Reg. 1.1402(a)-2(h)(3) would shield all the LLP's income from SE tax was plainly wrong.<sup>12</sup>

## The Tax Court's Analysis

The court disagreed with the partners' position. It reasoned that a limited partnership has two fundamental classes of partners, general and limited. General partners typically have management power and unlimited personal liability. Limited partners lack management powers but enjoy immunity from liability for debts of the partnership. Indeed, it is generally understood that a limited partner could lose his limited liability protection were he to engage in the business operations of the partnership.<sup>13</sup> Consequently, the interest of a limited partner in a limited partnership generally is akin to that of a passive investor.

In contrast, all partners of an LLP enjoy limited liability protection and may have management powers. In essence, an LLP is a state law general partnership that affords a form of limited liability protection for all its partners by filing a statement of qualification with the appropriate state authorities. In Kansas, an LLP is formed under the Kansas Uniform Partnership Act, which governs general partnerships. A Kansas partnership that elects to become an LLP continues to be the same entity that existed before the filing of a statement of qualification under the applicable Kansas LLP statutory provision.

The Tax Court observed that Section 1402(a)(13) was originally enacted (as Section 1402(a)(12) by P.L. 95-216, 12/20/77) at a time before entities such as LLPs were contemplated, and the statute did not, and still does not, define a "limited partner." When LLPs (and LLCs) began to be frequently used, it was determined that there needed to be a definition of "limited partner" for purposes of the SE tax. In 1997, Treasury issued Prop. Reg. 1.1402(a)-2, which was intended to do just that.<sup>14</sup>

The court stated that Prop. Reg. 1.1402(a)-2 ignited controversy, and that as a result, Congress enacted legislation providing that "[n]o temporary or final regulation with respect to the definition of a limited partner under section 1402(a)(13) ... may be issued or made effective before July 1, 1998."<sup>15</sup> As of 2005 (the most recent tax year at issue in *Renkemeyer*), neither Congress nor Treasury/IRS had issued any other pronouncements with respect to the definition of a limited partner for purposes of SE tax. The court therefore found itself "left to interpret the statute without elaboration."

Since Section 1402(a)(13) does not define "limited partner," the court said it would apply accepted principles of statutory construction to ascertain congressional intent: "It is a well-established rule of construction that if a statute does not define a term, the term is to be given its ordinary meaning. ... The court 'look[s] to the legislative history to ascertain Congress' intent if the *statutory purpose* is obscured by ambiguity."<sup>16</sup>

We pause here to consider the meaning of the court's language. The *statutory purpose* of Section 1402(a)(13) is not "obscured by ambiguity"—the purpose clearly is to exclude from NEFSE the distributive share of income of a "limited partner" (but not to exclude his payments under Section 707(c) for services actually performed for the partnership). The statutory purpose seems clear from the statutory language. Similarly, the ordinary meaning of the phrase "limited partner" is clear, under state law: it is one who is a limited partner of a partnership formed and operating under a state limited partnership act.

The “ambiguity” in *Renkemeyer* is this: for purposes of Section 1402(a)(13), does the phrase “limited partner” mean:

- (1) One who is a limited partner under state law (i.e., a limited partner in a state law limited partnership or LLLP; members of all other LLEs be damned),
- (2) One who has all, some, or one of the major characteristics of a limited partner (e.g., limited liability; no apparent or actual authority to participate in the partnership’s business operations; no actual participation in the control or management of the partnership’s business; and/or no actual participation in the partnership’s business operations), *regardless of* the underlying purpose or intended scope of the operative Code provision or Regulation at hand),
- (3) One who has all or some or one of the aforementioned characteristics of a limited partner that are *relevant* to the underlying purpose or intended scope of the operative tax provision at hand (here, Section 1402(a)(13) ), or
- (4) Something else altogether?

We would have less trouble with the *Renkemeyer* court’s reference to looking to legislative history to ascertain Congress’s intended meaning of “limited partner” if the Tax Court had not tied the test to “the statutory purpose” being “obscured by ambiguity.” Instead, we think the court should merely have stated that the failure of Congress (and Treasury, with respect to unperfected Regulations) to define “limited partner” required the court to determine the phrase’s meaning and scope for tax purposes consistent with the purpose of the statute as demonstrated by its legislative history. But we are not the court and the court is not us; so we return to the court’s analysis.

The court stated (without authority) that “limited partner” is a “technical term which has become obscured over time because of the increasing complexity of partnerships and other flowthrough entities as well as the history of section 1402(a)(13).” The court therefore concluded it had to look to the legislative history for guidance. Significantly, none of the taxpayer’s or Service’s briefs discussed the legislative history of Section 1402(a)(13) or gave any mention of it as being relevant in determining who is a “limited partner” or a “general partner” for purposes of that provision.

The insight gleaned by the court from the legislative history was that Section 1402(a)(13) was intended to ensure that individuals who merely invested in a partnership and who were not actively participating in the partnership’s business operations (which, the court noted, was the archetype of limited partners at the time) would not receive credits toward Social Security coverage. The relevant legislative history stated that the purpose of excluding the limited partner’s distributive share of partnership income or loss from the trade or business of a limited partnership “*is to exclude for coverage purposes certain earnings which are basically of an investment nature.*”<sup>17</sup> According to the court, the legislative history of Section 1402(a)(13) does not support a holding that Congress contemplated excluding from liability for SE taxes partners who performed services for a partnership in their capacity as partners (i.e., acting in the manner of self-employed persons).

Aside from a nominal amount of income, all of the law firm’s revenues were derived from legal services performed by the three individual partners in their capacities as partners. Thus it was clear to the court that the partners’ distributive shares of the law firm’s income did not arise as a return on the partners’ investment and were not “earnings which are basically of an investment nature.” Instead, the attorney-partners’ distributive shares arose from legal services they performed on behalf of the law firm partnership.

The Tax Court held that the respective distributive shares of the three attorney-partners arising from the legal services they performed in their capacity as partners in the law firm were subject to SE taxes for the 2004 and 2005 tax years.

**Summary.** To summarize and synthesize the reasoning of the Tax Court, in order of its presentation in the opinion:

- (1) As a general rule, each partner must include his distributive share of partnership income in calculating his NEFSE.
- (2) Section 1402(a)(13) provides an exclusion from the general rule with respect to certain types of partnership income of a “limited partner.”
- (3) It is the taxpayer’s burden to prove that he should be treated as a “limited partner” under Section 1402(a)(13).
- (4) In determining how to classify the (active) members of a Kansas LLP for tax purposes, it is recognized for state law purposes that the LLP is a general partnership that affords a form of limited liability protection for all its partners.
- (5) Section 1402(a)(13) was enacted before entities such as LLPs were contemplated.
- (6) Section 1402(a)(13) did not, and still does not, define a “limited partner.”
- (7) LLPs began to be frequently used in the 1990s, and it was determined that there needed to be a definition of “limited partner” for purposes of Section 1402(a)(13).
- (8) As of the tax years in question (i.e., 2004-05) and to date, Congress, Treasury, and the IRS have provided no guidance with respect to the definition of “limited partner” for purposes of Section 1402(a)(13), so the court must “interpret the statute without elaboration.”
- (9) Since Section 1402(a)(13) does not define “limited partner,” the term is to be given its ordinary meaning.
- (10) If the statutory purpose is obscured by ambiguity, the court will look to the legislative history to ascertain Congress’s intent.
- (11) “Limited partner” is a “technical term which has become obscured over time” because of (a) the increasing complexity of partnerships and other flowthrough entities (i.e., LLEs) and (b) the history of Section 1402(a)(13).
- (12) Because the term “limited partner” has become “obscured” over time, the court will look to legislative history for guidance.<sup>18</sup>
- (13) The legislative history reveals that the intent of Section 1402(a)(13) was to ensure that individuals who merely invested in a partnership (i.e., whose “earnings are basically of an investment nature”) and who were not actively participating in the partnership’s business operations would not receive credits towards Social Security coverage.
- (14) Conversely, the legislative history of Section 1402(a)(13) does not support a holding that Congress contemplated excluding partners who performed services in their capacity as partners on behalf of the partnership from liability for SE taxes.
- (15) The attorney-partners’ distributive shares arose from legal services they performed on behalf of the law partnership (and did not arise as “earnings which are basically of an investment nature”). Therefore, the attorney-partners’ distributive shares of the LLP’s income were subject to SE taxes.

## THE CASE'S IMPACT FOR 1402(a)(13) PURPOSES

What is the impact of *Renkemeyer* in characterizing members of LLEs as “limited partners” or “general partners” for purposes of Section 1402(a)(13) ? The Tax Court opinion does not purport to cover members of LLEs other than the three attorneys whose cases were before the court. Nevertheless, its reasoning as synthesized above indicates the following:

1. The court is applying the Section-by-Section Approach,<sup>19</sup> as it is limiting its review of legislative history and administrative developments (i.e., the Proposed Regulations) and analysis solely to Section 1402(a)(13). The court is not applying the Comprehensive Approach<sup>20</sup>; it clearly is not trying to divine a characterization of the terms “limited partner” and “general partner” applicable to all Code and Regulations provisions.
2. Similarly, the court is not using *Renkemeyer* as a podium from which to announce a global definition of the terms “limited partner” and “general partner” for all purposes of the Code and Regulations.
3. Notwithstanding arguments on brief by the taxpayer and the IRS<sup>21</sup> that Section 469 and Regulations and cases thereunder (particularly the Tax Court’s opinion in *Garnett*, 132 TC 368 (2009)) support the parties’ respective positions as to whether the taxpayer is a “limited partner” under Section 1402(a)(13), the Tax Court in *Renkemeyer* makes no reference to Section 469 or its Regulations. The court thereby clearly is signaling that its analysis under Section 1402(a)(13) is not affected by or *in pari materia* with the passive activity loss rules’ interpretation as to who are general or limited partners.

On brief, the taxpayer in *Renkemeyer* looked to Section 469 and Regulations and cases thereunder (to support its position that these LLP members were “limited partners” under Section 1402(a)(13) )<sup>22</sup> for the following propositions:

(a) Although Section 1402(a)(13) refers to a “limited partner” rather than a “limited liability partner,” its applicability should not be limited to only those entities formed pursuant to a (state law) limited partnership statute. According to the taxpayer’s brief, the Tax Court in *Garnett* made it clear that the partners of an LLP could be deemed “limited partners” for purposes of Section 469, regardless of the point that the partnership was not formed under state law as a limited partnership.

(b) The attorney-partners in *Renkemeyer* each held general managing interests and investing partner interests. Temp. Reg. 1.469-5T(e)(3)(ii) makes a distinction in a situation where one person holds both types of interests. It is imperative that the analysis of whether an interest is that of a “general partner” or “limited partner” is to be conducted separately for each type of interest. If it is determined that participation in management is a material factor in the analysis under Section 1402(a)(13), then the investing partner interests should be deemed to be a “limited partner” interest because they did not carry the ability to participate in management.

(c) Temp. Reg. 1.469-5T(e)(3) provides a definition of “limited partner” for purposes of the application of Section 469(h)(2). This definition provides an interest will be deemed to be a limited partnership interest if either it (i) is designated as such pursuant to its organizational documents, or (ii) actually enjoys limited liability pursuant to relevant state law. If this definition were used in the determination of whether Renkemeyer and his attorney-partners hold interests as a “limited partner,” *all* their interests arguably would be deemed to be interests of a “limited partner” because they would meet both tests in Temp. Reg. 1.469-5T(e)(3), although only meeting one of the two tests is required.

(d) The Tax Court’s ultimate holding in *Garnett* is that the partner in the LLP was deemed to be a “general partner.” Nevertheless, without the existence of a statutory exception such as that provided in Temp. Reg. 1.469-5T(e)(3)(ii)<sup>23</sup> (which applies when one owns both a general partner and limited partner interest), the interests of an LLP member should be deemed to be the interests of a “limited partner,” and *Garnett* arguably would have so held.

(e) The question at hand is whether the characteristics of the LLP interest formed under a given state's law, for purposes of any specific federal tax law provision, is an interest of a "general partner" or a "limited partner." That was also the focus of *Garnett* (decided under Section 469 ).

(f) The court in *Garnett* addressed two characteristics (in analyzing whether the interests were limited or general partner interests under Section 469): limited liability and participation in management. Petitioner's investing partner interests had both characteristics indicative of a "limited partner," as they had limited liability protection (as LLP members) and they provided the holder with no right to participate in management, which is indicative of a limited partner.

As one might expect, the IRS viewed the relationship of Sections 1402(a)(13) and 469 in a different light than did the taxpayer. The Service on brief looked to Section 469 and the Regulations and cases thereunder,<sup>24</sup> and raised the following propositions:

(a) If a partner is a general partner in a partnership, the exclusion under Section 1402(a)(13) (for limited partners) does not apply even if such general partner's interest is passive for purposes of Section 469.

(b)(i) The question presented by the taxpayer's opening brief is whether the Section 469 Regulations, *Garnett*, or Prop. Reg. 1.1402(a)-2 allow the taxpayer's partners to avoid SE tax on their share of the taxpayer's income under the limited partner exception in Section 1402(a)(13). The taxpayer's brief makes two arguments to support its assertion; one is that the Regulations under Section 469 as interpreted by the Tax Court in *Garnett* allow the attorney-partners in *Renkemeyer* to be classified as "limited partners" for purposes of Section 1402.

(ii) The taxpayer's reliance on the Section 469 Regulations is inapposite; the passive activity loss rules under Section 469 are neither expressly nor constructively applicable to the definitions for SE tax purposes under Section 1402. While both Section 469 and Section 1402 distinguish between general partners and limited partners, the distinction serves different purposes in each section.

(iii) The court's reasoning in *Garnett* actually militates *against* the taxpayer's arguments. In determining the meaning of "limited partner" for purposes of Section 469, *Garnett* noted that the primary difference between a limited partner and a general partner was that a general partner can participate in the management, but a limited partner cannot do so without losing its limited liability protection. *Garnett* ultimately held that ownership interests in the LLPs and LLCs at issue in that case had enough indices of general partnership interests that they were not interests in limited partnerships as limited partners under Temp. Reg. 1.469-5T(e)(3)(i) by operation of the general partner exception in Temp. Reg. 1.469-5T(e)(3)(ii). Accordingly, the *Garnett* holding is not helpful to the taxpayer's argument that its partners were limited partners for purposes of SE taxes.

In summary, and notwithstanding extensive briefing on point, the Tax Court in *Renkemeyer* without discussion refused to get into the question of whether and how Section 469 and *Garnett* might affect the analysis under Section 1402(a)(13). Indeed, the court's sole citation of *Garnett* was as partial support for the statement that, in essence, an LLP is a general partnership that affords a form of limited liability protection for all its partners by filing a statement of qualification with the appropriate state authorities. If one were a cynic, one might think the court's citation of *Garnett* was merely to signal readers of the opinion (including an appellate court, should the taxpayer have chosen to appeal) that the Tax Court was aware of *Garnett*—and chose to ignore (presumably as irrelevant) all other aspects of that opinion, for purposes of the case at hand.

4. The court is serving notice that for purposes of Section 1402(a)(13), it is not constrained by prior congressional or administrative actions (subsequent to enactment of that section in 1977) in ascertaining the meaning of the terms.<sup>25</sup>

5. The court analyzed the legislative history of Section 1402(a)(13) and came up with the following guidance: those intended to be “limited partners” for purposes of Section 1402(a)(13) are those who merely invest in the partnership and are not actively participating in the partnership’s business operations. Conversely, if the partner’s distributive share arises from services performed in his capacity as a partner, on behalf of the partnership, and *not* as “earnings which are basically of an investment nature,”<sup>26</sup> he will be treated as *not* a “limited partner.” (Presumably, that taxpayer *a fortiori* will be treated as a general partner.)

6. Referring back to the potential factors we previously identified<sup>27</sup> that might distinguish limited and general partners (including unlimited or limited liability to third parties; rights to participate in the management (or activity) of the partnership’s business; actual level of participation (or activity) in the entity’s business operations; and apparent or actual authority to bind the partnership), we see that the Tax Court expressly rejected the taxpayer’s contention that limited liability is the *sine qua non* of being a limited partner for purposes of Section 1402(a)(13) and instead adopted an “actual participation in the business operations” approach to distinguishing limited and general partners under that provision.

7. In applying a test based on (active) participation in the partnership’s business operations, the court did not distinguish (and was not required to do so by the facts and circumstances of the case) among the different levels of activity or participation by a member of an LLE as identified in Part 1 (i.e., active participation in management under Section 464; material participation under Section 469 ; active participation under Section 469; significant participation under Section 469; material participation under Section 1402; or some other measure of significant services or participation). 28

8. Neither the taxpayer, the government, nor the Tax Court in *Renkemeyer* made reference to the definitions of “general partner” and “limited partner” that may be found in the 2010 Instructions for Form 1065, which the IRS provides for taxpayers and return preparers to use in preparing partnership tax returns. The Instructions define a “general partner” to be “a partner who is personally liable for partnership debts.” A “limited partner” is defined to be “a partner in a partnership formed under a state limited partnership law, whose personal liability for partnership debts is limited to the amounts of money or other property that the partner contributed or is required to contribute to the partnership.” The 2010 Instructions further provided that “[s]ome 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*.” [Emphasis added.] 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).<sup>29</sup>

The Instructions for Form 1065 do not appear to advance the analysis for purposes of LLP members, including the attorney-partners in *Renkemeyer*. The LLP members arguably would not be “general partners” under the Instructions because they are not “a partner who is personally liable for partnership debts,” given the LLP shield. Nor would the LLP members be “limited partners” because they are not “a partner in a partnership formed under a state limited partnership law,” as LLPs are formed under a state general partnership act. Moreover, the Instructions state that some members of “other entities,” which might include LLPs, “may be treated as limited partners for certain purposes.” Those purposes conceivably could include Section 1402(a)(13)—but that section (unlike Section 469) was not expressly identified in the 2010 (and earlier) Instructions. Thus, the Form 1065 Instructions are not of much help or relevance to the situation in *Renkemeyer*.

## UNANSWERED QUESTIONS UNDER 1402(a)(13) AFTER RENKEMEYER

The reasoning of *Renkemeyer* leaves open many questions with respect to characterizing members of LLEs for purposes of Section 1402(a)(13), including the following:

**1. Factors.** Exactly what factors are being applied by the court to sustain SE tax liability in *Renkemeyer*? As described above, the court determined the status of the attorney-partners as general partners under state law, implying the State Law Characterization Approach is (still) the test in defining “limited” and

“general” partners for tax purposes. But the court also looked at the facts and circumstances, held them up against the perceived legislative history of Section 1402(a)(13), and found that the attorney-partners were acting as general partners. The latter effectively is the Section-by-Section Approach Based on the Operative Provision’s Underlying Purpose, discussed in Part 1.<sup>30</sup> It is unclear whether it was both factors or either one independently that led the court to its conclusion; a high-ranking IRS official recently pronounced the decision as being “a little murky” on that point.<sup>31</sup> (A “little murky” is a big understatement.)

**2. Source of partnership’s income.** What (if any) is the relevance of the nature or level of the partnership’s business operations? *Renkemeyer* involved a law firm LLP whose revenues and income (other than a nominal amount) were attributable to the rendering of services. Does the nature of the partnership’s income-producing activities affect the analysis of whether the partner’s distributive share of partnership income is NEFSE?

An individual’s dividends on stock, interest income, rental income, capital gains and losses, and gains and losses from the sale or other disposition of property not used in a trade or business are excluded from NEFSE pursuant to Section 1402(a). Such excluded income is not from a trade or business. It is clear that a partner’s distributive share of income from a partnership whose income comes from such sources is similarly exempted from NEFSE.<sup>32</sup> Thus, for example, if the *Renkemeyer* firm received stock for services (not subject to substantial risk of forfeiture) and such stock later generated dividend income for the partnership and ultimately capital gains on the stock’s disposition,<sup>33</sup> the attorney-partners in *Renkemeyer* could not have NEFSE on *that* stock dividend and capital gains portion of their partnership income, even if they had made no capital investment in the law firm and solely rendered services to the partnership so long as they were partners.

It has been recognized that *Renkemeyer* does not directly discuss the situation of an active partner in a business in which capital and services are both responsible for generating the LLE’s income. One article concludes that the likelihood is that the partner’s active participation would cause the income of the partner’s entire interest to be subject to NEFSE, although it could be argued that the partner’s interest should be bifurcated between the “active” interest and the “investor” interest.<sup>34</sup> Your author would vote for bifurcation in this scenario as being the more equitable answer, although it often would be difficult to administer in practice.

Consider a partnership that generates its income from a trade or business other than services (e.g., the sale of widgets), and has no dividend, capital gain, interest, or rental income that by definition is excludable from NEFSE. Unlike the law firm partnership in *Renkemeyer*, the source of the widget partnership’s income is not solely or predominantly services. Indeed, capital may be a material, a principal, the principal, or the predominant income-producing factor for such a partnership. Under the rationale of *Renkemeyer*, is each partner’s allocable share of such income included in or excluded from NEFSE for the partners?

The Tax Court in *Renkemeyer* did not have before it, and did not address, a non-service partnership that did not generate income from rendering services. The court’s opinion does state that the *Renkemeyer* law firm’s revenues were derived from legal services, but does not make the nature of the partnership’s income critical to its analysis. Rather, the court observes that all but a nominal amount of the law partnership’s income derived from legal services performed by the attorney-partners in their capacities as partners. The court focused on the services the partners performed (on behalf of the partnership), and the fact that the partners’ distributive shares arose from such services, rather than from the partners’ investment.

*Query* whether the court’s analysis logically should apply equally if the partnership generated its income from business operations other than the rendering of services, so long as the partner rendered services (on behalf of the partnership) in his capacity as a partner. The *Renkemeyer* opinion does not speak (in dictum or otherwise) to the potential characterization as NEFSE of a distributive share of income of a service-rendering LLP member whose tax partnership generates its revenues and income solely, predominantly, principally, or even materially other than from services.

Instead, we would look to existing Regulations for the answer. Reg. 1.1402(a)-2(d) provides in relevant part that an individual's NEFSE includes, in addition to the earnings from a trade or business carried on by him, his distributive share of such income or loss, described in Section 702(a)(9) (now Section 702(a)(8) ), from *any trade or business carried on by each partnership of which he is a member*.<sup>35</sup>

**3. Contributions of services and capital.** What is the relevance of a service partner's having made more than a nominal capital contribution to the partnership?

If the attorney-partners in *Renkemeyer* had substantial (rather than nominal) capital invested in the partnership, would the court still have determined that all of the partners' income was NEFSE? If not, what would be the court's methodology for determining what part of their income is deemed NEFSE? Would the court bifurcate the member's distributive share of the LLE's income as NEFSE in part? Or would the court apply an "all or nothing" test, e.g., is the partner's distributive share of partnership income deemed attributable primarily to (1) the partner's service activity, in which case the court might rule that *all* of the partner's distributive share of income from the partnership is subject to NEFSE, or (2) the partner's investment, in which case the court might rule that *none* of the partner's income is subject to NEFSE?

If an "all or nothing" test were applied, might this test be based on the partner's share of partnership income being deemed (1) "predominantly from services," (2) "not predominantly from services," (3) "predominantly from investment," or (4) "not predominantly from investment"? Might the performance of *any* services for the tax partnership cause the partner's entire distributive share of the partnership's income to constitute NEFSE? As a variant, might the performance of any services by the partner *other than* those rendered in exchange for a guaranteed payment (of an appropriate amount) for services under Section 707(c) cause the partner's entire distributive share to constitute NEFSE?

It is unclear where the boundaries lie. The *Renkemeyer* court concluded that all of the partners' income was NEFSE although "each contributed a nominal amount (\$110) for their respective partnership units." (This would fall into either the "predominantly from services" or the "not predominantly from investment" alternatives posited above.) The court gave no indication of how it would have measured NEFSE if more than a nominal amount of capital had been contributed by the attorney-partners.

Although the court in *Renkemeyer* does not speak to the situation involving a member who contributes both capital and services to or on behalf of the LLP, it does provide an important piece of the puzzle. *Renkemeyer* in part stands for the proposition that for purposes of Section 1402(a)(13), the legislative history of P.L. 95-216 that pertains to Section 1402(a)(13) provides insight that can be used in the absence of Regulations or other guidance. The court was focusing on the legislative history in its efforts to define "limited partner" for NEFSE purposes. Nevertheless, additional legislative history of P.L. 95-216 (not quoted in the opinion) that supports bifurcation of the partner's distributive share for NEFSE purposes deals with a dual-status partner (which, both then and now, is permissible under state partnership law):

"Distributive shares received as a general partner would continue to be covered. Also, if a person is both a limited partner *and* a general partner in the same partnership, the distributive share received as a *general* partner would continue to be covered under present law." (Emphasis added.)

It is fair to infer from the quoted sentences that for purposes of Section 1402(a)(13)<sup>36</sup> the distributive share received by the dual-status partner as a limited partner will not be covered under present law (i.e., treated as NEFSE), but rather subject to the new (post-1977) rule (whereby the limited partner's distributive share is not subject to NEFSE). That dichotomy was undoubtedly in recognition of the traditional difference between general and limited partners under state partnership law—which, as we know from the other legislative history discussed herein, is meant to differentiate interests whose earnings are basically of an investment nature from those attributable to one who (through his partnership interest) is actively participating in the partnership's business operations.

Thus, one could conclude from *Renkemeyer*'s reliance on the legislative history of Section 1402(a)(13) that if the LLE (other than a state law limited partnership<sup>37</sup>) creates two classes of interests or units (one denominated Capital Interests, which are issued to its members solely in exchange for capital contributions, and the other denominated Service Interests, issued solely in exchange for services),<sup>38</sup> the IRS arguably should characterize the Capital Interests as "limited partner" interests and the Service Interests as "general partner" interests for purposes of Section 1402(a)(13).

The 1997 Proposed Regulations under Section 1402(a)(13) expressly allow for bifurcation of interests where one holds more than one class of interest in a partnership. Pursuant to Prop. Reg. 1.1402(a)-2(h) (3), a partner could be treated as both a limited partner and a general partner in the same partnership for purposes of Section 1402(a)(13). The bifurcation rule is designed to exclude from NEFSE those amounts of a partner's allocable share of income that are "demonstrably returns on capital invested in the partnership."<sup>39</sup> Thus, although *Renkemeyer* does not address multiple classes of interests for NEFSE purposes, dual-class partners can for the time being rely on the 1997 Proposed Regulations if they so choose to permit bifurcation as dealt with therein. High-ranking IRS officials have informally so stated on several occasions, both before and after the *Renkemeyer* opinion was handed down.<sup>40</sup>

The harder case is where the member of the LLE receives a single LLE interest in exchange for both capital and services. Would the IRS permit or require the member to bifurcate his interest into two, with part of the interest being subject to NEFSE and part not subject? How would the bifurcation be done? Assuming there is more than one reasonable method of computing the member's bifurcated shares of partnership income, what method(s) can or must be used?

Several potential administrative problems for taxpayers and the IRS can arise under either permissible or mandatory bifurcation scenarios. Indeed, the proposed tax legislation on carried interests received for services (which would enact new Section 710) has wrestled with definitional and administrative issues pertaining to ascertaining service-related income from income attributable to investments, while being subject to substantial criticism on substantive grounds.<sup>41</sup>

The ABA Section of Taxation in 1999 and 2011 submitted proposals along these lines. In 1999 the ABA, working closely with the AICPA's Tax Division, submitted a proposal recommending Congress amend Section 1402 to provide that income of owners of tax partnerships (including LLCs) that is attributable to capital not be subjected to SE taxes. Last December the ABA Section of Taxation submitted its "Options for Tax Reform in the Partnership Tax Provisions of the Internal Revenue Code," which recognized that the statutory language of Section 1402(a)(13) does not give definitive guidance to partners who provide both services and capital to a tax partnership to determine what portion of their income is subject to SE tax liability. The ABA Tax Section recommended consideration of amending Section 1402(a)(13) "to focus on whether income is attributable to services provided or capital contributed to a partnership (rather than state law labels) and to provide that income that is attributable to capital is not subject to [SE tax]." Under the ABA's proposed legislative solution (which presumably would eliminate rather than clarify the meaning of the terms "limited partner" and "general partner"), "Treasury would be given the regulatory authority to provide clear rules and safe harbors under this section."

**4. Treatment of LLC members.** Many law firms (and countless service businesses) operate as LLCs. Would the Tax Court's analysis in *Renkemeyer* be extended to members of LLCs as well? As discussed below, we believe it would.<sup>42</sup>

**5. Applicability to state partnership law limited partners.** If the *Renkemeyer* court were faced with a limited partner of a state law limited partnership (instead of a member of an LLP, which is a state law general partnership whose partners have limited liability protection), would the court have applied its "earnings from investment/earnings from services performed for the partnership in one's capacity as a partner" distinction to find state law limited partners not to be "limited partners" for purposes of Section 1402(a)

(13) ? That would be a bold move, in light of the Sense of the Senate Resolution and the congressional/regulatory tempest back in 1997-98<sup>43</sup> when Treasury attempted to apply a 500-hour participation test in differentiating “limited partners” from “general partners” under Prop. Reg. 1.1402(a)-2. The Tax Court opinion in *Renkemeyer* refers to those Proposed Regulations as having “ignited controversy.” But courts must rule on matters both controversial and mundane, and the language in the opinion clearly does not rely on state law labels to determine when one who is a member of a tax partnership must be characterized as a limited or general partner for purposes of Section 1402(a)(13).

The argument that *Renkemeyer* should be extended to state partnership law limited partners can be based on the case’s rationale that looks to the source of the partner’s share of partnership income, i.e., from services performed for the partnership or from earnings on the investment in the partnership. That rationale arguably maintains that individuals who are limited partners (and render services to the partnership) under state law may not be able to rely on Section 1402(a)(13) to argue that they are not liable for SE taxes. Curtis Wilson, IRS Associate Chief Counsel (Passthroughs & Special Industries), informally stated after *Renkemeyer* was decided that such an approach is consistent with the intent of the statute. Finding *Renkemeyer* to be “consistent with what I think the statute intended,” Wilson reportedly said that “if you read the rationale, it’s not limited to [a Kansas LLP] necessarily.”<sup>44</sup>

Moreover, Wilson’s immediate predecessor, William O’Shea, who is now in private practice, reportedly noted the potential application of *Renkemeyer* to some state law limited partners. Before *Renkemeyer*, even conservative tax advisors at the Big Four accounting firms would recommend that if you were (solely) a state partnership law limited partner, your allocable share of partnership income would not be subject to characterization as NEFSE (even if you rendered services, presumably). Under *Renkemeyer*, even limited partners under state partnership law may be subject to NEFSE on their distributive share of income in that they may not meet the limited partner exception under Section 1402(a)(13), according to O’Shea.<sup>45</sup> Our esteemed colleagues Bob Keatinge and Jim Sowell, who are both well-versed in LLEs and SE taxes, also view *Renkemeyer* as potentially applying to state law limited partnerships.<sup>46</sup>

The application of *Renkemeyer* to the allocable shares of income of some state partnership law limited partners is by no means clear, however. As discussed in Part 1, case law prior to *Renkemeyer* under Section 1402(a)(13) focused solely on the status of the partner as (or not as) a limited partner under applicable state partnership law.<sup>47</sup> Those cases disregarded how active or passive the partner was, and did not employ a test based on whether the putative limited partner obtained his partnership interest for services rendered for the partnership. One commentator reads the *Renkemeyer* dicta on the legislative history as “a bit of an outlier,” and suggests still going back to the earlier cases<sup>48</sup> for someone who is “really a limited partner in a state law limited partnership.”<sup>49</sup>

But the weight of the authority of *Renkemeyer* could cast a pall over this area of the law for state law limited partnerships. Because *Renkemeyer* is a Tax Court regular opinion, while two of the contrary cases are Tax Court memorandum opinions<sup>50</sup> and the third is a district court case,<sup>51</sup> one commentator has correctly concluded that the Tax Court regular opinion arguably should be given greater weight than the three other decisions.<sup>52</sup> A court directly encountering that situation might conclude that the meaning of “limited partner” in Section 1402(a)(13) indeed must be given its ordinary meaning—and the face of the statute clearly refers to a “limited partner” exemption from NEFSE.

In 1977, when Section 1402(a)(13) (then Section 1402(a)(12)) was enacted, it was typically the case that a “limited partner” was one so named in a validly formed and operated state law limited partnership. The basic and expressly stated premise of *Renkemeyer*, namely that “limited partner” is “a technical term which has become obscured over time because of the increasing complexity of partnerships and other flowthrough entities,” does not ring true for state partnership law limited partnerships, particularly those that do not take advantage of the liberalized provisions of recent versions of limited partnership acts that permit a broad range of services to be rendered by their limited partners.

Simply stated, a future court may find *no* uncertainty as to whether a “vanilla” limited partner in a limited partnership organized under a state’s limited partnership act is a “limited partner” as described in Section 1402(a)(13), and therefore the court will not need to (and perhaps may not be permitted to) “look to the legislative history for guidance,” as the Tax Court did in *Renkemeyer*. We may recall Justice Potter Stewart’s comments about pornography: “... perhaps I could never succeed in intelligibly [defining hard-core pornography]. But I know it when I see it....”<sup>53</sup> For state partnership law limited partners, the better saying may be, “it’s easy to define (i.e., a limited partner of a validly formed and operated state law limited partnership) *and* I know it when I see it.”

In identifying the fundamental differences between general partners and limited partners, the Tax Court stated that general partners typically have management power and limited partners lack management powers.<sup>54</sup> Indeed (according to the court) it is generally understood that a limited partner could lose his limited liability protection for debts of the partnership “were he to engage in the business operations of the partnership.” The court’s citation of authority for this latter proposition is not on point.<sup>55</sup> Indeed, we know of no authority that holds a limited partner could lose his limited liability protection solely for engaging in the business operations of the partnership. The opinion totally disregards the important distinction between limited partners “lacking management powers” or “not participating in the control of the business,” on the one hand, and “not engaging in the business operations of the partnership,” on the other.

Another argument for excluding state partnership law limited partners from being categorized as “general partners” under Section 1402(a)(13), even if they participate in the partnership’s business operations, can be based on former Section 512(b)(13). Before its repeal in 1976, that section provided for an exclusion from unrelated business income (UBI) for certain trusts holding limited partner interests; the exclusion was unavailable if the trust “was (or was liable as) a general partner in such partnership.”<sup>56</sup> Former Section 512(b)(13) proves that when Congress means to address the tax consequences of a limited partner who becomes liable as a general partner, it can and will expressly do so. Congress has *not* chosen to do so (i.e., delineate among state law limited partners) in other Code provisions.

Former Section 512(b)(13) arguably is relevant to the scope of Section 1402(a)(13) because it demonstrates Congress’s ability and willingness to deal with hyperactive limited partners who become liable as general partners for taking part in control of the business, and to provide them with the same tax consequences that general partners receive (rather than consequences befitting limited partners)—for purposes of former Section 512(b)(13) only. That section did not and would not impose a “general partner’s” tax consequences on a limited partner who merely performed services for his partnership in his capacity as a partner or who actively participated in the partnership’s business operations.

Although this little-known provision was never interpreted in Regulations or case law, its legislative history indicates that the restrictions as to the limited partner who took part in the control of the partnership were intended to ensure that the income received would be wholly passive in character, and that the trust’s charitable tax exemption would not be used for unfair business competition.<sup>57</sup> Thus, if such a testamentary trust violated ULPA section 7, it henceforth lost its exclusion on UBI because of the inapplicability of former Section 512(b)(13).

To the best of your author’s knowledge, prior to its 1976 repeal former Section 512(b)(13) was (and to this day remains) the only provision in the Code recognizing that a limited partner may take part in control of the partnership’s business (so as to become liable as general partner) and that tax consequences (i.e., the exclusion of or the inclusion in income as UBI) can result from that putative limited partner’s level of activity. As former Section 512(b)(13) is the only known provision of the Code to deal with a breach of the enacted state partnership law versions of ULPA section 7, it could have provided guidance on questions involving whether the limited partner’s violation of ULPA section 7 (and its successor provisions in ULPA (1976), ULPA (1976) with 1985 amendments, and ULPA (2001)) will cause him to be deemed a general partner for some or all other federal tax purposes.

Unfortunately, the language of the statute, regarding whether the limited partner “was (or was liable as) a general partner,” is somewhat ambiguous and is arguably of no precedential value in this sense. The repealed statute can be read for the proposition that on at least one occasion Congress explicitly recognized that for tax purposes a state law general partner was not identical to a limited partner liable (for state law purposes) as a general partner, as it referred to both.<sup>58</sup>

**6. Applicability to a withdrawn or retired LLE member who continues to get Section 736 payments.** A partner who withdraws or retires from the LLE for state law purposes is still treated as a tax partner pursuant to Reg. 1.736-1(a) until he receives his final partnership payment in liquidation of his partnership interest. For purposes of Section 1402(a)(13), that partner’s receipt of Section 736(a) payments is treated as NEFSE unless the payments meet the requirements of Section 1402(a)(10), which is another exception to the general rule of Section 1402(a) that all of the income allocated by a tax partnership to a tax partner is NEFSE.

The retired or withdrawn partner may be providing few or no services to the tax partnership in his capacity as a partner after retirement or withdrawal, but he nonetheless may be allocated partnership income. Would the activity-related test in *Renkemeyer* be interpreted to mean the Section 736 payments are not subject to NEFSE because at the time of allocation of the income to the retired partner he is not actively providing services to the partnership? If so, can that result be reconciled with Section 1402(a) —and specifically Section 1402(a)(10), which indicates that a retired partner’s allocable income from the tax partnership is indeed NEFSE unless the payments are periodic retirement payments to a retired partner who complies with the stringent conditions of Section 1402(a)(10) and Reg. 1.1402(a)-17?<sup>59</sup>

Note the tension between the “source of income” (services or investment) analysis of *Renkemeyer* and the approach in Reg. 1.1402(a)-17(c)(1), which effectively provides the retired partner recognizes NEFSE (i.e., he does not meet the exclusion of Section 1402(a)(10)) *even if* he renders no services with respect to any trade or business carried on by the partnership during the partnership’s relevant tax year, if the retired partner does not meet certain additional requirements, e.g., pertaining to repayment to him of partnership capital. Nothing in *Renkemeyer* indicates that the Tax Court considered the tension with Section 1402(a)(10) and Reg. 1.1402(a)-17 that is created by its holding.

**7. Obscure terms.** Are “limited partner” and “general partner” really technical terms that have been obscured? The *Renkemeyer* opinion states that “limited partner” is a technical term (for tax law purposes) that has become obscured over time because of the increasing complexity of partnerships and other flowthrough entities as well as the history of Section 1402(a)(13). A co-drafter of Prop. Reg. 1.1402(a)-2 observed that the court did not need to raise the specter of ambiguity based on changing “conditions” (e.g., the evolution of state LLE acts) because previous court decisions found no ambiguity about the plain meaning of the term “limited partner.”<sup>60</sup> Those prior decisions were issued during 1990-2000, a period when LLCs and LLPs were coming into widespread use.

On the other hand, even if the meaning of “limited partner” has become obscured over time, is the converse equally true, i.e., is “general partner” a technical term for tax purposes that similarly has “become obscured over time because of the increasing complexity of partnerships”? In light of *Renkemeyer*, can a “general partner” for purposes of Section 1402(a)(13) be defined only as “a partner (for tax law purposes) who is not a limited partner (for tax law purposes)?” Would the *Renkemeyer* court characterize a state partnership law general partner in a state law limited partnership as a “limited partner” for purposes of Section 1402(a)(13) so as to *not* have NEFSE if the partner has a substantial capital investment in the partnership and does not actively participate in the partnership’s business operations or perform services for the partnership in his capacity as a partner?

And what would be the result under the Tax Court’s analysis in *Renkemeyer* if the state law *general* partner of a state law *general* partnership has a substantial equity investment in the partnership but does not actively participate in the partnership’s business operations? Could he be treated as a “limited partner”

(for tax purposes) of a state law general partnership (at least for purposes of NEFSE under Section 1402(a)(13) )? Isn't there something wrong with that picture? A respected commentator queries whether the Tax Court's two-prong test in *Renkemeyer* of mere investment and absence of active participation in the entity's business operations means that, in the extreme, partners in a general partnership could be characterized as "limited partners" under Section 1402(a)(13).<sup>61</sup>

**8. State law.** Why didn't the Tax Court in *Renkemeyer* decide the case under the State Law Characterization Approach? The IRS argued on brief, clean and simple, that the exception in Section 1402(a)(13) exception applies only to limited partners; under Kansas law, there are no limited partners in an LLP; therefore, the attorney-partners in the *Renkemeyer* law firm were not "limited partners" for purposes of determining SE tax.

We found nothing in the taxpayer's briefs to negate this contention. We found nothing in the Service's briefs to indicate its contention required a Section-by-Section Approach so as to invoke the legislative history of Section 1402(a)(13). Could a future court that does not wish to divine the legislative intent of Section 1402(a)(13) in an LLE situation that is not satisfactorily answered by *Renkemeyer*'s analysis merely apply the State Law Characterization Approach, take note that the attorney-partners in *Renkemeyer* would have been subject to SE taxes under that approach, and declare the *Renkemeyer* analysis of legislative history to be mere dictum? We find it ironic that the usual uncertainty in determining whether a member of an LLC is more like a "general" partner or a "limited" partner was not present in *Renkemeyer*—in this case, it was clear under state law that the attorneys were general partners as members of a Kansas LLP.

**9. The Proposed Regulations.** Does the analysis in *Renkemeyer* cast further doubt on the authority of the 1997 Proposed Regulations? One commentator reportedly observed that the Tax Court in *Renkemeyer* merely gave a passing mention to the Proposed Regulations, which in her view is further evidence that they carry no weight.<sup>62</sup>

Another commentator has concluded that *Renkemeyer* casts doubt on the authority of Prop. Reg. 1.1402(a)-2, based on the court's statement that it was left to interpret the statute "without elaboration" because neither Congress nor the IRS has issued any pronouncements in the area since the moratorium on finalizing the Proposed Regulations.<sup>63</sup> That commentator recognizes, however, that Proposed Regulations are considered "authority" for determining whether substantial authority exists for purposes of the Section 6662 substantial underpayment penalty, and that courts have on occasion sustained taxpayer reliance on Proposed Regulations (even if the IRS imposes a different final Regulation detrimental to the taxpayer who acted in reliance on the "most reasonable interpretation" of the issue available to the taxpayer at the time his return was filed).<sup>64</sup> Moreover, it is recognized that IRS officials have informally said that taxpayers can continue to rely on the 1997 Proposed Regulations and that a reasonable position that is within the four corners of the Proposed Regulations will not be challenged; but that such informal statements do not constitute authority.<sup>65</sup>

We recognize that Proposed Regulations, much less informal statements by Service officials, do not constitute "authority" for purposes of Section 6110(k), but we take some comfort that (unless and until reversed) favorable IRS statements involving reliance on the Proposed Regulations even after the *Renkemeyer* opinion<sup>66</sup> will carry weight on audit or appeal, as a practical matter.

Two years before *Renkemeyer*, the Tax Court in *Garnett* made a passing reference to the 1997 Proposed Regulations, but gave no indication that those Proposed Regulations constituted authority any different from other Proposed Regulations. In observing that the Code and Regulations provide no general definition of "limited partner," the *Garnett* court commented in footnote 19 of its opinion that solely for purposes of Section 1402(a)(13) and the Regulations thereunder, Prop. Reg. 1.1402(a)-2(h) defines "limited partner."<sup>67</sup> Footnote 19 provides no deference to that Proposed Regulation, and does not discuss Congress's temporary moratorium on those Regulations. The Tax Court clearly had the opportunity in *Garnett* to do either or both, if it so desired.

**10. Impact of final Regulations.** If Prop. Reg. 1.1402(a)-2 were finalized in form substantially similar or identical to the 1997 version, would the Tax Court view that Regulation as expressly addressing members of LLPs (as in *Renkemeyer*) and LLCs? The Tax Court does not deal with that question in its *Renkemeyer* opinion. In footnote 19 of its opinion in *Garnett*, however, the Tax Court states that Prop. Reg. 1.1402(a)-2(h) “do[es] not expressly address the treatment of an L.L.P. or L.L.C. member.”

## **POTENTIAL 1402(a)(13) IMPACT ON MEMBERS OF VARIOUS TYPES OF LLEs**

What tax consequences would follow if the court’s analysis in *Renkemeyer* was applied to the classification of members of various types of LLEs as “limited” or “general” partners for purposes of Section 1402(a)(13) ? Paragraphs 1-5 below discuss the categorization of members of LLPs; 6-10 analyze the characterization of members of LLCs; 11-15 analyze members of state law limited partnerships; 16-20 analyze the members of LLLPs; and 21-25 cover the members of state law general partnerships as being “limited” or “general” partners under Section 1402(a)(13). It is assumed for this portion of the article that *Renkemeyer* was not decided on the basis of the state law characterization of the law firm’s LLP as a general partnership, but rather under the court’s analysis of “legislative intent” described above.

**1. Active members of other law firm LLPs.** The position taken by the attorney-partners in *Renkemeyer* was at best aggressive; it is difficult to contend that partnership earnings consisting entirely of fees for professional services performed by the members of an LLP (i.e., a state law general partnership) should be exempt from SE tax. Indeed, under the 1997 Proposed Regulations (on which taxpayers can rely, according to current IRS informal statements) the attorney-partners in *Renkemeyer* would not have been characterized as “limited partners”—Prop. Reg. 1.1402-2(h)(5) expressly provides that a service partner in a service partnership cannot be a “limited partner” for purposes of Section 1402(a)(13).

It is practically certain that active members of other law firms organized in Kansas as LLPs will be subject to SE tax on all of their distributive share of their law firms’ income (that is not otherwise excludable from NEFSE under Section 1402(a) ) under *Renkemeyer*. For federal tax purposes capital has not been viewed as a material income-producing factor in law partnerships; it is the rendering of services which is the dominant source of a law partnership’s income. It is hard to envision an active member of another law firm LLP organized in Kansas being able to distinguish his case from *Renkemeyer*.

It also is practically certain that active members of law firms that are LLPs not organized in Kansas would be subject to SE taxes on all of their income under *Renkemeyer*. The preceding analysis should apply equally to law firm LLPs organized in any of the other 50 jurisdictions; there is nothing unusual about the Kansas LLP statute. Moreover, the court’s decision in *Renkemeyer* did not turn on the specific provisions of the Kansas LLP statute.

**2. Active members of service LLPs (other than law firms).** It is highly likely that active members of other service firms organized and operating as LLPs also would be subject to SE taxes on all of their allocable income from the LLP under the analysis in *Renkemeyer*. The partners of a service partnership who render services as accountants, doctors, consultants, engineers, or actuaries (among others), and who contribute no significant amounts of capital, would be viewed by the Tax Court as having their distributive shares of income arising from services they performed on behalf of the partnership and not arising as earnings that are basically of an investment nature.

Some service partnerships require extensive amounts of capital for equipment, software, and other tangible and intangible property essential to the service partnership’s operations. Some service partnerships have partners who do not render significant services, but rather are entirely or predominantly investors providing capital, to the partnership.<sup>68</sup> These types of LLPs appear distinguishable from the predominantly service-based law partnership LLP in *Renkemeyer*. Should the treatment of such investor-partners be different (i.e., not subject to SE tax), even though the source of income for their LLPs is clearly service-generated

(in whole or predominant part)? Under *Renkemeyer*, the distributive share of those investor-partners' income from the LLP would not be subject to SE tax, even though those LLP members are general partners for state law purposes.

**3. Inactive members of law (or other service) LLPs.** It would appear that under *Renkemeyer* inactive members of law (or other service) LLPs, i.e., those who do not perform services to or on behalf of the LLP, might be characterized as "limited partners" for purposes of Section 1402(a)(13). If so categorized, their distributive share of income from the LLP would not be NEFSE, even though LLP members are general partners for state law purposes.

An analysis of this scenario under the rationale of *Renkemeyer* requires us to determine exactly why the LLP member is receiving an allocable share of partnership income, given his status as an inactive partner. Is he a formerly active attorney (or other service provider) who has left all or a portion of his partnership capital in the partnership, but otherwise is partially or fully retired? If so, one might conclude his allocable share of income is in effect a redemption (or series of payments in liquidation) of his LLP interest that is governed by Section 736.

As discussed above,<sup>69</sup> under *Renkemeyer* that might be sufficient to characterize his share of income as not subject to NEFSE because he is a limited partner for purposes of Section 1402(a)(13). Nevertheless, that categorization seems to directly clash with Section 1402(a)(10), which excludes from NEFSE only those retirement payments to former state law partners that meet that section's stringent conditions; all other retirement payments would be NEFSE.<sup>70</sup>

If the inactive partner is not withdrawing all of his capital in the LLP, and he is not a retired partner whose payments are governed by Section 736, his distributive share of income could be excluded from NEFSE under the court's analysis in *Renkemeyer*. Assume the law partner is disabled and is being allocated income pursuant to his law firm's (self-insured) practice or policy to pay an amount up to six months' income<sup>71</sup> for temporarily or permanently disabled partners. Under *Renkemeyer*, would that income be NEFSE because the individual is actively participating in the partnership's business operations (he is not), or would it be excluded from NEFSE because his earnings during the disability period "are basically of an investment nature" (they are not), or does *Renkemeyer's* principled analysis just fail to deal with this particular situation? The answer is unclear.

**4. Members of LLPs whose members provide capital but not services.** Although the LLP form is most frequently used by professional service firms, some LLPs are engaged in other businesses or activities. In these non-service LLPs, some or most of the members invest capital but do not provide services to or on behalf of the partnership. Under the *Renkemeyer* rationale, such capital-investing partners would be treated as limited partners, and thereby not have NEFSE from the LLP, because their earnings from the LLP would be of an investment nature. In that event, those LLP members—who clearly are general partners for state partnership law purposes—would be treated as other than general partners for purposes of Section 1402(a)(13).

**5. Members of LLPs whose members provide capital and services.** *Renkemeyer* provides no meaningful guidance on how to characterize an LLP member who provides both capital and services to or on behalf of the partnership. As discussed in "Unanswered Questions," number 2, above, it is unknown whether the court would treat (1) all of the partner's distributive share as NEFSE, (2) none of the partner's share as NEFSE, or (3) some portion of his share of LLP income as NEFSE, and if so, how that portion is determined.

As described in "Unanswered Questions," number 3, above, *Renkemeyer* does provide one piece of the puzzle when determining NEFSE when a member contributes both capital and services. If the LLP has two classes of interests (e.g., capital interests and service interests) and the LLP member receives

capital interests with respect to his capital contribution(s) and service interests in exchange for services rendered or to be rendered to the LLP, *Renkemeyer* and the legislative history of Section 1402(a)(13) provide support for treating the partner's distributive share of LLP income attributable to the capital interests as not subject to NEFSE and his distributive share of income attributable to the service interests as subject to NEFSE.<sup>72</sup>

**6. Active members of law firm LLCs.** The discussion in paragraphs 1-5 above relates to classification of LLP members as "limited" or "general" partners under Section 1402(a)(13). Would the court's analysis in *Renkemeyer* be extended to members of LLCs as well? Paragraphs 6-10 deal with members of LLCs in fact patterns similar to those earlier posited as to the impact of *Renkemeyer* on classification of LLP members as "limited" or "general" partners for purposes of Section 1402(a)(13).

As described in paragraph 1, under the *Renkemeyer* analysis active members of law firm LLPs clearly will be subject to SE tax on their distributive shares of their law firms' income (not otherwise excludable from NEFSE under Section 1402(a)). Your author believes the analysis in *Renkemeyer* would be extended to members of LLCs as well. More important, unofficial comments of a then-high-ranking IRS official strongly hint that this will be the Service's position.<sup>73</sup>

**7. Active members of service LLCs (other than law firms).** As described in paragraph 2, under the *Renkemeyer* analysis it is very likely that active members of service firms organized and operating as LLCs also will be subject to SE taxes on all of their allocable income from the LLC. The members of such LLCs typically do not contribute significant capital and their distributive shares of income arise from services they performed on behalf of the LLC, rather than as earnings that are basically of an investment nature.

As described in paragraph 2, some service entities (including LLCs) require extensive amounts of capital that is essential to the LLC's operations. Some service LLCs have members who do not render significant services, but who are akin to investors providing capital to the LLC. These types of LLCs appear distinguishable from the service-based law firm LLP in *Renkemeyer*. If investor-partners in a service-based LLP are not wholly subject to SE tax on their LLP income, then the investor-members in a service-based LLC should not be wholly subject to SE tax on their LLC income, either. *Renkemeyer* does not deal with these situations.

**8. Inactive members of law (or other service) LLCs.** It would appear that under *Renkemeyer* inactive members of law (or other service) LLCs might be characterized as "limited partners" for purposes of Section 1402(a)(13). The analysis in paragraph 3 above would seem equally applicable to the same situations discussed therein if LLCs were involved.

**9. Members of LLCs whose members provide capital but not services.** In LLCs that are engaged in businesses or activities other than professional services, some or most of the members solely invest capital. Under the *Renkemeyer* rationale, these capital-contributing members would be treated as limited partners, and thereby not recognize NEFSE from their allocable share of the LLC's income, because they render no services and their earnings would be of an investment nature.

**10. Members of LLCs whose members provide capital and services.** *Renkemeyer* provides no significant guidance on how to characterize an LLC member who provides both capital and services to or on behalf of the LLC. It is unknown whether the court would treat (1) all of the member's distributive share as NEFSE, (2) none of the member's share as NEFSE, or (3) some portion of his share of LLC income as NEFSE, and if so, how that portion is determined.

As described in paragraph 5 above, *Renkemeyer* provides one piece of the puzzle when a member contributes both capital and services. If the member receives one class of interest (capital interests) in the LLC with respect to his capital contribution and a second class (service interests) in exchange

for services rendered or to be rendered to the LLC, *Renkemeyer* and the legislative history of Section 1402(a)(13) provide support for treating the member's distributive share of LLC income attributable to the capital interests as not being NEFSE and his share of income attributable to the service interests as being NEFSE.

**11. Active members of law firm limited partnerships.** Paragraphs 11-15 respond to the question whether the court's analysis in *Renkemeyer* would be extended to members of state law limited partnerships, and if so, in what circumstances.

In light of the uncertainty of the potential impact of *Renkemeyer* on state law limited partnerships and their state partnership law limited partners described earlier,<sup>74</sup> it is unclear whether *Renkemeyer* will be extended to cause active members in a law firm limited partnership to have SE tax liability. Taken to its logical extreme, the rationale of *Renkemeyer* would cover state law limited and general partners in law firm limited partnerships if they render services to or for the benefit of the partnership and have made no substantial investment of capital in the firm. But would a court hold some or all of the state law limited partners to be general partners for tax purposes under this rationale? In absence of Regulations on point, we think not.

**12. Active partners in service limited partnerships (other than law firms).** Would *Renkemeyer* apply to limited and/or general partners in a state law limited partnership whose predominant source of revenues comes from rendering services other than legal services? *Renkemeyer* does not involve a state law limited partnership; the case addresses members of an LLP (i.e., a state law general partnership). With respect to state law limited partners who actively render services for their partnership, the potential impact of *Renkemeyer* is uncertain for reasons described earlier.

*Renkemeyer* does not address state law general partners in a state law limited partnership. It is not likely that active general partners who receive their interests in a service limited partnership for rendering services on behalf of or to the partnership (and who make no significant capital contributions to the partnership) would be characterized under Section 1402(a)(13) as "limited partners" under the rationale of *Renkemeyer* or the case law that pre-dates *Renkemeyer*.

**13. Inactive members of law (or other service) limited partnerships.** As the scope of *Renkemeyer* is unclear with respect to state law limited partnerships, it is difficult to predict whether the rationale of *Renkemeyer* would be applied to characterize "inactive" general partners of a limited partnership as "limited partners." The discussion in paragraph 3, above, would seem applicable here, as well.

**14. Partners in a state law limited partnership whose members provide capital but not services.** Under the *Renkemeyer* rationale, such capital-investing partners (be they limited or general partners not rendering services) would be treated as "limited partners," because their earnings from the LLP would be of an investment nature. In that situation, it would follow that those passive general partners—who clearly are general partners for state partnership law purposes—would be treated as other than general partners for purposes of Section 1402(a)(13).

**15. Members of a state law limited partnership whose members provide capital and services.** *Renkemeyer* provides no meaningful guidance on the characterization of a partner (general or limited) who provides both services and capital to the limited partnership in exchange for his partnership interest. The discussion in paragraph 5, above, seems equally applicable in this scenario.

**16. Active members of law firm LLLPs.** If the application of the rationale in *Renkemeyer* is unclear with respect to partners in a state law limited partnership, how would the case be applied to the general and limited partners of an LLLP, formed under the provisions of a state statute designed to provide limited liability protection to the general partner (as well as the limited partners) in the LLLP? Paragraphs 16-20 address this question.

With respect to active members of a law firm LLLP, be they general or limited partners under state partnership law, if their allocable share of the LLLP's income derives from services they render to or for the benefit of the LLLP and not from their investment in the LLLP, they are likely to be subjected to SE tax if the rationale of *Renkemeyer* is applied. The applicability of SE tax to the general partner(s) of a law firm LLLP would come as no surprise, notwithstanding their limited liability protection under the LLLP provisions. Indeed, such LLP members are functionally identical to the LLP members in the *Renkemeyer* case, i.e., they are state law general partners with limited liability protection who provide services to or on behalf of their LLP/LLL, while making no significant capital investments.

The more difficult case again would be the limited partners of the law firm LLLP who render services but contribute insignificant capital to the LLLP. They are functionally similar to the state law limited partners who render services to their limited partnership described in paragraph 11, above. As capital is not deemed a material income-producing factor in a law firm taxable as a partnership and the limited partners in the LLLP make no substantial capital contribution (and thus do not look to their investment in the firm as the source of their earnings from the LLLP), the rationale of *Renkemeyer* could apply, as a technical matter. (Would a court do so under the circumstances? Again, we think not.)

**17. Active members of service LLLPs (other than law firms).** Would the rationale of *Renkemeyer* apply to limited and/or general partners in a state law LLLP whose revenues predominantly come from rendering services other than legal services? We think the answer again is uncertain. As stated above, *Renkemeyer* does not involve a state law limited partnership; an LLLP is a form of limited partnership. It is likely that active general partners of an LLLP who receive their interests in a service LLLP for services rendered to or on behalf of the LLLP (and make no significant capital contributions to the LLLP) would not be characterized under Section 1402(a)(13) as "limited partners" under the rationale of *Renkemeyer* or pre-existing case law. Nevertheless, the potential impact of *Renkemeyer* on state law limited partnerships (and thereby, LLLPs) is uncertain, for reasons described earlier.

**18. Inactive members of law (or other service) LLLPs.** As the scope of *Renkemeyer* is unclear with respect to state law limited partnerships, it is again difficult to predict whether the case's rationale would be applied to characterize "inactive" general partners of an LLLP as "limited partners." The discussion in paragraph 3, above, would seem applicable here as well.

**19. Members of LLLPs whose members provide capital but not services.** Under the rationale of *Renkemeyer*, a member of an LLLP who invests capital and looks to it for his or her allocable share of the LLLP's income would be treated as a "limited partner." It would logically follow that any passive general partners of the LLLP—albeit general partners for state partnership law purposes—would be treated under *Renkemeyer* as other than general partners for purposes of Section 1402(a)(13).

**20. Members of LLLPs whose members provide capital and services.** As discussed in paragraph 5, *Renkemeyer* provides no meaningful guidance on the characterization of a partner (limited or general) who provides both services and capital to the LLLP in exchange for his partnership interest.

**21. Active members of law firms that are state law general partnerships.** Although the taxpayers in *Renkemeyer* were members of an LLP (and thus had a limited liability shield not available to other general partners), there is nothing in *Renkemeyer* to indicate the court would not apply the same rationale to a state law general partnership that is not an LLP. Paragraphs 21-25 deal with this application of *Renkemeyer*.

Even if the rationale of *Renkemeyer* is theoretically applicable to members of a state law general partnership, it seems clear that an active general partner in a law firm general partnership will be deemed a "general partner" for SE tax purposes. Indeed, *Renkemeyer* involved a state law general partner who was a member of a state law general partnership (LLP), and was held not to be a "limited partner" for

purposes of Section 1402(a)(13). The *Renkemeyer* rationale—that if the partner provides services to the partnership and does not look to his (de minimis) investment for his earnings from the partnership—would reach the right result here: the general partner’s income from the partnership will be NEFSE.

**22. Active partners in service firms (other than law firms) that are state law-general partners.** Under the rationale of *Renkemeyer*, active members of other service firms organized and operating as state law general partnerships would be deemed “general partners” for SE tax purposes, if they contribute no significant amounts of capital. Such partners would be viewed by the Tax Court as having their distributive shares of income arising from services they performed on behalf of the partnership, and not arising as earnings that are basically of an investment nature.

Some partners in service firms that are general partnerships also contribute substantial capital to their partnerships. The discussion in paragraph 2, above, is relevant to analyzing whether *Renkemeyer* would apply in a case involving a state law general partnership that is not an LLP.

**23. Inactive members of law (or other service) firms that are state law general partnerships other than LLPs.** As the scope of *Renkemeyer* is similarly unclear with respect to state law general partnerships (other than LLPs), it is difficult to determine whether the rationale of the case would be applied to characterize “inactive” general partners of the general partnership as “limited partners.” The discussion in paragraph 3, above, would seem applicable here as well.

**24. Partners in a state law general partnership whose members provide capital but not services.** Prior to *Renkemeyer*, the law was seemingly clear: a general partner in a state law general partnership was subject to NEFSE, even if he rendered no services and did not partake in management of the partnership.<sup>75</sup> But those cases are not of strong precedential value, and the court in *Renkemeyer* made no reference to them.

If a general partner renders no significant services to or for the benefit of the partnership, but makes a substantial capital contribution to the partnership, *Renkemeyer* would indicate the state law general partner should be characterized as a limited partner for purposes of Section 1402(a)(13). The case’s rationale is that the capital-investing partners (albeit clearly general partners for state law purposes) will generate their earnings from the general partnership from their investments. In that scenario, it would follow under *Renkemeyer* that those passive state law general partners would be treated as other than general partners for purposes of SE tax liability.

Would a court so hold? Or, is it more likely that a court would distinguish *Renkemeyer* (even though *Renkemeyer* also involved a state law general partnership (which was an LLP))? Only time will tell.

**25. Members of a state law general partnership whose members provide capital and services.** *Renkemeyer* provides no substantial guidance on the characterization of a general partner who provides both services and capital to a state law general partnership in exchange for his partnership interest. The discussion in paragraph 5, above, seems equally applicable in this scenario.

## **RAMIFICATIONS FOR OTHER ‘LIMITED PARTNER’ AND ‘GENERAL PARTNER’ PROVISIONS**

The implications of *Renkemeyer* for purposes of defining “limited partner” and “general partner” under Code provisions other than Section 1402(a)(13) remain unclear. The Tax Court opinion expressly limits its analysis and holding to Section 1402(a)(13), as described earlier. No court case is known to have since cited *Renkemeyer*, and the Service has not (to our knowledge) made express reference on brief to *Renkemeyer* or issued any administrative guidance citing or based on *Renkemeyer* inside or outside of Section 1402(a)(13).

It is difficult to predict whether the court's method of analysis in *Renkemeyer* pertaining to investigation of the legislative intent of the operative Code provision will be adopted and applied outside Section 1402(a)(13). If *Renkemeyer's* discussion of legislative history is mere dictum, then *Renkemeyer*, narrowly read, merely holds that state law partnership labels are dispositive—an LLP member is a general partner for state law purposes; state law labels control; and therefore the attorney-partners were not and could not be “limited partners.” This State Law Characterization Approach, if applied beyond Section 1402(a)(13), would thereby clarify the status of LLP and LLLP members for purposes of all provisions of the Code and Regulations, with the corresponding advantages and disadvantages discussed earlier of adopting that approach.<sup>76</sup>

On the other hand, the dicta in *Renkemeyer* calling for an inquiry, in the absence of final Regulations on point, into the legislative intent of the operative Code provision (here, Section 1402(a)(13) ) could be applied to other sections, as well. The Section-by-Section Approach, based on the operative provision's underlying purpose,<sup>77</sup> was effectively applied by the Tax Court in *Renkemeyer*. This approach has its own merits and demerits. It is unknown whether *Renkemeyer's* methodology will be applied by other courts under other Code and Regulations provisions (notwithstanding the Section-by-Section Approach being mere dicta in *Renkemeyer*).

The impact of *Renkemeyer* beyond Section 1402(a)(13) may be indirectly felt. Prior to the case, it was believed by many (if not most) that the undefined terms “limited partner” and “general partner” had a meaning based on state law characterization. Much like Dorothy pulling back the Wizard of Oz's curtain to reveal a mere, fallible mortal, *Renkemeyer* may have freed up Treasury and the IRS to re-examine the operative meaning of “limited partner” and “general partner” beyond the state law characterization curtain. If that is *Renkemeyer's* legacy, then the case's impact will be felt far beyond Section 1402(a)(13) ; the dicta (i.e., look to legislative intent, in absence of Regulations or other guidance on point) would have become the rule.

## CONCLUSION

The uncertainty as to the meaning of “limited partner” and “general partner” predates *Renkemeyer*, as discussed in Part 1. Four decades ago, your author called for clarification as to the characterization for various operative federal tax purposes of a tax partner who for state law purposes exhibited some of the characteristics of a general partner and some of the characteristics of a limited partner. We identified several definitional approaches that could be taken under the myriad Code sections and Regulations that used either or both of the terms (to no avail). In 1996, the ABA Section of Taxation submitted its suggested approach to Treasury and the IRS to comprehensively define “limited partner” and “general partner” (to no avail). In 1999, the ABA Section of Taxation (working closely with the AICPA's Tax Division) submitted a legislative proposal to amend Section 1402 to obviate the need for definitional distinctions between “limited partners” and “general partners” (to no avail). In 2001, the JCT Staff submitted for congressional consideration, in its Tax Simplification Report, its recommendation to modernize references to “limited partner” and “general partner” (to no avail). Thus, even before *Renkemeyer*, the score was Confusion 4, Clarification 0.

*Renkemeyer* compounds the confusion in characterizing members of LLEs because it reaches the right result, but for the wrong reason. It was a perfectly selected case for the IRS to litigate; what judge would allow active attorney-partners (in a state law general partnership, no less) to avoid SE taxes on their law firm's operating income?<sup>78</sup>

Nevertheless, the scope, breadth, validity of analysis and impact of *Renkemeyer* remain unclear. The case sheds light on how the Tax Court dealt with a futile effort by an active member of a (law firm) service partnership (LLP) to avoid SE tax. In so doing, the court gave no indication that the meaning of “limited partner” and “general partner” under other Code or Regulations provisions, or cases (like *Garnett*) interpreting those other provisions, have any impact in interpreting those terms under Section 1402(a)(13).

*Renkemeyer* creates more heat than light. As to the “heat,” it has been reported (perhaps overzealously) that *Renkemeyer* “has sent ... shock waves through the legal and accounting communities”<sup>79</sup> and “through the tax bar.”<sup>80</sup> A former high-ranking IRS official has been quoted as saying *Renkemeyer* “is probably the most aggressive I’ve ever seen the Tax Court.”<sup>81</sup>

A lively debate as to the fiscal and political fallout of *Renkemeyer* flared shortly after the opinion was published.<sup>82</sup> One commentator observed that many law and accounting firm partners pay no employment taxes on their share of the firm’s income because they take the position that they are limited partners exempt from SE tax under Section 1402(a)(13). That commentator (dubiously, in our view) quantified the potential impact of *Renkemeyer* as exceeding \$1 billion in SE taxes—from legal and accounting service firms alone.<sup>83</sup> A group of attorneys and accountants, finding the commentator’s article to be “offensive,” heatedly disagreed with their nemesis’s premises, calling their antagonist’s position that the annual loss of revenue exceeds \$1 billion a year “a bold statement that might raise some eyebrows and the attention of revenue hungry government officials.”<sup>84</sup>

But rather than belabor *Renkemeyer*’s potential (welcomed or unwelcomed) heat on the matter, let’s look for light (or at least enlightenment). Does the case point the pathway to perdition or rather plunge perplexed practitioners, preparers, and taxpayers into profound confusion? Initial reports were that *Renkemeyer* brought even greater uncertainty.<sup>85</sup> After having prepared this exhaustive (and exhausting) two-part article, we concur. As discussed earlier,<sup>86</sup> our unanswered questions include:

- The (still undefined) meaning of “limited partner” and “general partner” for purposes of Section 1402(a)(13),
- Whether the court’s interpretation of “limited partner” applies to all unincorporated pass-through entities under Section 1402(a)(13),
- Whether making a significant investment of capital is or is not a (or the) determinative factor,
- Whether rendering significant services to the tax partnership is or is not a (or the) determinative factor, and
- To what extent a member’s contribution of both capital and services affects the determination of his “limited partner” or “general partner” status.

The uncertainty wrought by *Renkemeyer* extends to state partnership law limited partners who participate in partnership operations, an activity permitted (albeit to a more limited extent than allowed today) even in 1977, when Section 1402(a)(13) was enacted. Under then-applicable partnership law, a limited partner could lose his limited liability were he to “take part in control of the business,” but that did not preclude a limited partner from rendering substantial services to his partnership (i.e., engaging in the business operations of the partnership) without becoming liable as a general partner. Thus, notwithstanding legitimate concerns voiced by respected partnership tax law experts about the penumbra of *Renkemeyer*,<sup>87</sup> strong arguments can be made that state law labels do apply with respect to state partnership law limited partners, despite the underlying rationale of *Renkemeyer* and its divining of the intent underlying the legislative history of Section 1402(a)(13).

The answer as to whether a state law limited partner recognizes NEFSE on his allocable share of partnership income awaits guidance and/or further litigation. Before *Renkemeyer*, the predominant view of knowledgeable tax practitioners was that the state law limited partner did not recognize NEFSE under Section 1402(a)(13) on his Section 704(b) distributive share of partnership income, even if he rendered services for the partnership. *Renkemeyer* creates confusion where none previously existed, as its two-prong test may conceivably apply to state law limited partners, not merely members of LLPs.

It is flat-out wrong to read *Renkemeyer* for the proposition that a partner who renders services to his or her tax partnership is automatically (or even presumptively) not a “limited partner” for federal tax purposes. Unlike those few other Code provisions that use the term “limited partner,” Section 1402(a)(13) expressly envisions the rendering of services by limited partners. Nevertheless, Section 1402(a)(13) provides that payments to the limited partner for services actually rendered to or on behalf of the partnership constitutes NEFSE only if (1) they are guaranteed payments described in Section 707(c) and (2) such payments are in the nature of remuneration for those services.

*Renkemeyer* states that the insight provided by the legislative history reveals that the intent of Section 1402(a)(13) was to ensure that “individuals who *merely* invested in a partnership and who were not actively participating in the partnership’s business operations” were not to have NEFSE. (Emphasis added.) We submit that the legislative history also reveals that a limited partner’s share of partnership income attributable to an interest he received for services actually performed by the limited partner for the partnership also *are not* NEFSE—*except* to the extent he received guaranteed payments as described in Section 707(c), such as salary and professional fees, from the partnership. Nothing in the legislative history indicates that state law limited partners who actively participate in the partnership’s business operations (but do not take part in the control of the business so as to be deemed a general partner or liable as a general partner) have SE tax liability on their Section 704(b) allocable shares of partnership income.

*Renkemeyer*’s method of analysis—i.e., resorting to and interpreting the legislative history of Section 1402(a)(13)—did not have the benefit of discussion on brief by the taxpayer or the IRS. None of the four filed briefs discussed the legislative history of Section 1402(a)(13) or gave any mention of it as being relevant in determining who is a “limited partner” or a “general partner” for purposes of that provision.

So, after all is said and done, how should we think about *Renkemeyer*, in a world of LLEs? The case clearly cannot be limited to its facts (i.e., active members of a Kansas service firm LLP)—no matter how much practitioners might wish it to be<sup>88</sup>—but it also should not be extended beyond logic and good sense. There is no reason to believe that Congress in 1977 did not intend the phrase “limited partner” to encompass limited partners in state law limited partnerships. Any attempt to broadly extend the rationale of *Renkemeyer* to members of state law limited partnerships should fail. Clearly, the statute itself unambiguously provides that limited partners can render services and (with the exception of guaranteed payments they receive for services) not be subject to SE tax. Rendering substantial services alone does not make one a “general partner” for tax purposes.

By the same token, *Renkemeyer* should not be extended to state law general partnerships. It is clear on the face of the statute that Section 1402(a)(13) does not apply to general partners. Rather, the long-standing rule (as provided in Section 1402(a) and the Regulations thereunder) that general partners are subject to SE tax liability on their allocable share of the partnership’s income is not affected by the analysis in *Renkemeyer*. The opinion purportedly focused on the “obscured” meaning of “limited partner.” The court did not state, nor is it logical to conclude, that “general partner” with respect to a state law general partnership is similarly “obscure” and therefore ambiguous so as to require inspection of the statute’s legislative intent, history, or purpose.

The treatment of members of LLPs is a closer question, as under state law they clearly are general partners, in which event the analysis of *Renkemeyer* did not need to go any further if state law characterization is determinative of a partner’s potential treatment under Section 1402(a)(13). Nevertheless, presumably because of the limited liability shield available to LLP members (under the LLP provisions of each state’s general partnership statutes), the court in *Renkemeyer* went further, in investigating whether such general partners having limited liability protection were “limited partners” as the phrase is used in Section 1402(a)

(13).<sup>89</sup> Rather than basing its analysis on state law characterization of LLP members as state law general partners, the court took upon itself a search for the legislative intent or purpose of the provision.

We do not quibble with the court's conclusion that the attorney-partners in *Renkemeyer* were subject to SE tax on their distributive share of income, under the facts, as they were general partners under state law. We do doubt that the court, in the absence of Regulations on point, should have sought to identify the perceived legislative intent when dealing with a state law partnership (LLP).

With respect to LLLPs, it similarly would follow that since the entity is a state law limited partnership, its limited partners clearly come within the scope of Section 1402(a)(13), even if they render services and their respective capital contributions to the LLLP are negligible. The state law characterization should control; if anything, limited partners in an LLLP are virtually identical to limited partners in a state law limited partnership that has not elected LLLP status under their applicable state statute.

The general partner of an LLLP, however, is more akin to a member of an LLP. He has the powers of a general partner under applicable state law (i.e., a general partner of a limited partnership, akin (but not identical) to the powers of a general partner of a general partnership). The liability of the general partner of an LLLP is limited, like that of a limited partner of an LLLP. If the *Renkemeyer* analysis is correct with respect to LLP members (i.e., to disregard the state law characterization label and analyze the member's level of services and his allocable share of partnership income from the earnings on his investment), a similar rule should apply for the general partner of an LLLP.

Finally, with respect to members of LLCs, Treasury threw in the towel with Prop. Reg. 1.1402(a)-2, in providing that LLC members could be limited partners or could be general partners for this tax purpose, depending on whether they meet or fail to meet certain standards described in the Proposed Regulations. It would be hard for Treasury to do a 180-degree reversal, and state that members of LLCs cannot be treated as "limited partners" under Section 1402(a)(13). Moreover, unlike the forms of state law general partnerships and state law limited partnerships in existence in 1977 when Section 1402(a)(13) was enacted, the characterization of LLCs (and their members) is uncertain, and the legislative intent/legislative history of Section 1402(a)(13) provide no reference to (then virtually unheard of) LLCs. This is the type of situation that *Renkemeyer's* analysis was meant to address—there was and is no state law general partnership or state law limited partnership label that automatically affixes to LLCs (unlike LLPs or LLLPs). Thus, if the rationale of *Renkemeyer* is to be extended beyond service firm LLPs, it would be logical to apply it to service firm LLCs as well.

It is self-evident that the characterization of members of LLEs for federal tax purposes is a long-standing problem with no broadly applicable legislative or administrative solution on the horizon. It is not for lack of effort by the tax bar. We first identified the definitional and operational problems in 1979,<sup>90</sup> back when only general and limited partnerships were in vogue. With the advent of LLCs, LLPs, and LLLPs, and revised/liberalized limited partnership acts becoming commonplace in the 1980s and 1990s, the need for guidance skyrocketed but practitioners' pleas have gone unanswered. The ABA Section of Taxation's LLC Task Force concluded in its 1996 ABA Comments that there would be enormous value in developing a comprehensive test for characterization of LLC members as general or limited partners.<sup>91</sup> The Task Force observed that in light of the number of Code and Regulations provisions implicated, it would be an administrative nightmare to develop and apply a separate characterization rule for each provision. Moreover, a comprehensive rule would be an opportunity for clarification and simplification. The ABA Task Force's suggested language for a proposed definitional Regulation under Section 7701 merits renewed examination, as the intervening years—as evidenced by *Renkemeyer* and recent cases under Temp. Reg. 1.469-5T—have done much to confuse matters further.

Perhaps we (and others) have grossly overestimated the likely impact of *Renkemeyer*. Perhaps, like Dorothy in the "Wizard of Oz," we can merely close our eyes, click our heels three times, and reawaken

in Kansas, rid of all our Renkemeyerian nightmares. But alas, from Kansas is where *Renkemeyer* sprung upon us all. No relief to be found there.

Yet all along we may have had the power to return from the land of *Renkemeyer* relatively unscathed—even without clicking our heels. We can merely dismiss the court’s analysis of legislative history as being mere dicta, and go back to relying on the State Law Characterization Approach or any of our other enumerated defensible ways to deal with the meanings of “limited partner” and “general partner.” A practitioner (who happens to be the former IRS official listed as the principal author of Prop. Reg. 1.1402(a)-2 ) reportedly observed that Judge Jacobs did not need to ascertain and discuss Congress’s intent in order to find for the government; he didn’t even need to raise the specter of ambiguity about the plain meaning of the term “limited partner.”<sup>92</sup> That practitioner concluded that many other practitioners will merely dismiss the Tax Court’s foray into the legislative intent or purpose as dicta, pending Treasury/IRS guidance or Congress’s changing the law.

### **What Needs to Be Done (We Hope)**

Indeed, in light of the *Renkemeyer* opinion, there are more voices calling for government action (be it by Treasury/IRS or by Congress) to address the ambiguities arising from (1) the use of LLEs that were not in existence when Section 1402(a)(13) et al. were enacted, with respect to the meaning of “limited partner” and “general partner,” and (2) the active roles taken by some state law limited partners which are permitted under applicable state law limited partnership statutes.<sup>93</sup>

And the call for guidance on this topic is loud and clear. After the issuance of *Renkemeyer*, the AICPA Tax Division classified guidance in the form of re-proposed or finalized Regulations as very high priority.<sup>94</sup> Other groups, firms, and commentators have trumpeted the call. Unfortunately, Treasury and the IRS did not place the topic of guidance on the meaning of “limited partner” and “general partner” for purposes of Section 1402(a)(13) on the Priority Guidance Plan for 2011-12.<sup>95</sup>

### **What Will Happen (We Think)**

Will the call be answered with a comprehensive solution that covers the Code’s and Regulations’ wide-ranging uses of the terms “limited partner” and “general partner”? We don’t see a Code-wide definition (e.g., one of the Comprehensive Approach alternatives discussed in this article) on the horizon. That would take rarely achieved coordination and cooperation of countless factions of Treasury, IRS, and (in light of the “heat” brought on by the 1997 Proposed Regulations) the staffs of Congress’s tax-writing committees. We have heard that the question of whether a Code-wide “uniform” definition would be the best approach was informally considered in connection with the preparation of the 1997 Regulations project under Section 1402(a)(13), and the consensus was there never would be a consensus reached inside the government on those definitions.

So what has *Renkemeyer* wrought? And what might we prognosticate will happen, post-*Renkemeyer*? We foresee the following:

1. Comprehensive, Code-wide definitions of “limited partner” and “general partner” will never be issued by Treasury or the IRS, nor will Congress enact them. (No pressure to do so; no glory in it, either.)
2. Treasury and the IRS will move forward in defining “limited partner” for purposes of Section 469(h)(2),<sup>96</sup> and will move to finalize Prop. Reg. 1.469-5(e) (public hearings held on 4/30/12) in substantially similar form.<sup>97</sup> The Proposed Regulation clearly is a response to several courts (including the Tax Court) that concluded the Regulation applies the wrong standards in classifying an LLC or LLP member as a “limited partner” for purposes of Section 469. But for those court decisions, the topic almost certainly would not have resurfaced for revision.

3. For purposes of Section 469, Treasury and the IRS will create a definition in Regulations that jettisons the “limited partner equals a partner with limited liability” standard in Temp. Reg. 1.469-5T(e) and adopt a standard that is better reconciled with the court cases under Section 469. That definition (as stated in the Preamble to REG-109369-10) will be expressly limited to applying solely for purposes of that Section. (Why? See item 1 in this list.)

4. Is *Renkemeyer* a game changer or just the same game with a different name? More specifically, does it abolish the concept that (in absence of Regulations or statutory language to the contrary) references in the Code and Regulations to “limited partner” and “general partner” are limited to their state law labels, at least in the case of members of state law general and limited partnerships (including LLPs and LLLPs)? The *Renkemeyer* opinion does not profess to speak beyond characterizing certain LLP members for purposes of Section 1402(a)(13), but the opinion’s statement that the meaning of “limited partner” has “become obscure” may be a pivotal point in future Tax Court cases interpreting the meaning of the term.

If the definition of “limited partner” is “obscure” under Section 1402(a)(13), is it any less obscure under all other Code and Regulations provisions that use the term? It is not clear whether Treasury and the IRS are now emboldened by *Renkemeyer* for purposes of Section 469—and other sections—to jettison the State Law Characterization Approach (and if so, to what extent) for classifying members of LLEs, and instead go to *Renkemeyer*’s “legislative intent” approach. Absent any further guidance from the courts, Treasury and the IRS may be so inclined. There are, however, major differences in the legislative intent and purposes of Sections 469 and 1402(a)(13), and the ultimate outcome under a “legislative intent” standard could be substantially different definitions for purposes of each section. Thus, the “limited partner equals a partner with no right to manage” standard may be adopted (as proposed) for purposes of Regulations under Section 469 (and Section 892<sup>98</sup>), but *not* used for purposes of Section 1402(a)(13), should Regulations be re-proposed (or the statute amended) for that purpose.

What is good for the goose may be good for the gander: if *Renkemeyer* emboldens the geese at Treasury and the IRS to divine the legislative intent of Code provisions other than Section 1402(a)(13) with respect to the definitions of “limited partner” and “general partner,” what precludes taxpayer-ganders from doing the same? We foresee taxpayers using *Renkemeyer* to similarly ferret out the meaning of “limited partner” (and “general partner”) for purposes of any and all other operative Code provisions by analyzing those provisions’ legislative intent—at least in those situations when it advances the taxpayers’ tax position to do so.

5. There is nothing conceptually wrong with a tax partner being deemed a “limited partner” for some operative Code provisions and a “general partner” for others. We expressed that view 33 years ago<sup>99</sup> and stubbornly adhere to it (even more so) today, in light of the *Renkemeyer* court’s search (in the absence of final Regulations on point) for the legislative intent underlying the case’s operative Code provision (Section 1402(a)(13)).

6. It remains unclear whether Treasury and the IRS will next (or ever) tackle issuance of final or re-proposed Regulations under Section 1402(a)(13), absent congressional action. If the Regulations move forward, will *Renkemeyer*’s operative approach (i.e., determining the “legislative intent”) be adopted? Will the IRS put its own spin on the meaning of the legislative intent under Section 1402(a)(13), to deal with the meaning of “limited partner” and “general partner” for the remaining numerous permutations of members of LLEs discussed above?<sup>100</sup>

If Treasury and the IRS do not move forward with guidance under Section 1402(a)(13), we anticipate that additional cases involving members of LLEs will percolate up through audits and ultimately lead to some court decisions (which may modify, limit, or even emasculate the approach the Tax Court took in *Renkemeyer*), particularly under differing facts and circumstances.

7. Other than the pending Proposed Regulations under Sections 469 and 892, we do not foresee in the near future any activity by the government to provide guidance regarding the meaning of “limited partner” and “general partner” for purposes of other Code or regulatory provisions. Treasury and the IRS have limited resources and they seem to be receiving little (if any) pressure to give guidance through Regulations projects under the remaining ten Code sections or 70-plus Regulations that use the terms “limited partner” and/or “general partner.”

8. If, however, Treasury and the IRS issue Regulations under specific Code provisions that provide definitions of “limited partner” and “general partner,” it is likely that the courts will bow to the definitions under recent Supreme Court precedent.<sup>101</sup> Congress has failed to define those terms by statute or to give explicit guidance as to their meanings in legislative history. In the litigated arena of Section 469(h)(2), several courts (like the *Renkemeyer* court) noted they were issuing their opinions in the absence of Regulations on point.

9. But are Treasury and the IRS going down the wrong path in proposing (and perhaps promulgating in final form) Regulations based on the “right to manage” (or lack thereof) for purposes of defining a “limited partner” under Sections 469(h)(2) and 892? As discussed in Part 1,<sup>102</sup> and in recent ABA and NYSBA reports,<sup>103</sup> it is not clear why a distinction based on rights to manage should be controlling and that standard will create its own discontinuities.

10. Absent regulations to the contrary, it is our view that the rationale in *Renkemeyer* is too broad to be applied to typical members of so-called “vanilla” state law limited partnerships and state law general partnerships. *Renkemeyer* does not give the government a “green light” to characterize all state law limited partners who provide significant services as being “general partners” under Section 1402(a)(13). Indeed, given the lack of clarity in the authorities discussed in this article for purposes of Section 1402(a)(13), applying the State Law Characterization Approach remains a reasonable route to treating state law limited partners as “limited partners” under Section 1402(a)(13). Moreover, at this juncture the position seems infused by substantial authority so as to advert a Section 6662 penalty, even if not ultimately determined to be the law.

11. LLC members by definition are not members of state partnership law limited partnerships or general partnerships. Until there is future case law refining *Renkemeyer* we might expect the IRS to give section-by-section guidance that will look to the differing tea leaves of legislative intent to determine the classification of LLC members as “limited partners” or “general partners” for purposes of each operative Code provision. Or we may see no guidance for decades, once the IRS promulgates new Section 469 and 892 Regulations that define a “limited partner” for their respective purposes.

12. Members of traditional service firms (e.g., lawyers, accountants, doctors, and actuaries) that operate in LLC form will most likely be characterized as “general partners” for almost all if not all operative Code and Regulations provisions. Such active members of service firms organized as LLCs will most likely have all of their allocable income from the LLC treated as NEFSE for purposes of Section 1402(a)(13) under any standard adopted. As the result in *Renkemeyer* reflects, we think the courts will find a way to subject such service-generated income to SE tax liability—even if the case’s rationale (like *Renkemeyer*’s) leads to a plethora of questions as to the characterization of other members of LLEs as “limited partners” or “general partners.”

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1. Banoff, “*Renkemeyer* Compounds the Confusion in Characterizing Limited and General Partners—Part 1,” 115 JTAX 306 (December 2011) (“Part 1”).

2. References herein to “state law” are to domestic entities only (e.g., state partnership law as determined under state statutes for the organization and operation of partnerships), and for simplicity’s sake include entities formed in the District of Columbia. References to state statutes or uniform acts adopted by the National Conference of Commissioners on Uniform State Laws (NCCUSL) are so identified herein. It is recognized that one may own more than one type of interest in a limited liability entity for state law purposes, e.g., as a limited partner and a general partner. References to “state

law” do not refer to state *tax* law, i.e., the tax law applied by states to characterize owners of LLEs for tax purposes or for determining those owners’ state income tax liabilities.

References to “limited partner(s),” “general partner(s),” and “limited” and “general” partners, when so designated in quotation marks, means those tax partners who are treated as such for federal tax purposes (regardless of their status for state law purposes). It is recognized that for federal tax purposes, one may hold interests as a “limited partner” and a “general partner” in the same tax partnership.

3. The state law evolution of general partnerships (which, of course, are the basis for state law “general partner” status) and LLEs are interwoven into Exhibit 1 of Part 1, “The ‘General Partner’ and ‘Limited Partner’ Timeline.”
4. The limitations on activities under the various uniform limited partnership acts (which are approved by NCCUSL) are laid out in Exhibit 2 of Part 1, “Limitations on Limited Partners’ Activities.”
5. Including (1) the State Law Characterization Approach; (2) the Comprehensive Approach with Uniform Application, where the comprehensive definition could be based on (a) unlimited or limited liability, (b) rights to participate in management (or activity) of the entity, (c) actual level of participation or activity in the entity’s business operations, (d) authority to bind the LLE, (e) effect of a member’s withdrawal, (f) notice to a member constituting notice to the LLE, or (g) fiduciary duties owed by one partner to another; (3) the Comprehensive Approach With Specified Exceptions; (4) the Comprehensive Approach Based on State Law Characterization With Exceptions; (5) the Section-by-Section Approach Based on the Operative Provision’s Underlying Purpose; (6) the Section-by-Section Approach Based on Date of Enactment; (7) Characterized by the Source of the Member’s Allocable Share of Income (Capital and/or Services); (8) Characterized by Deference to Treasury/IRS Guidance in Prop. Reg. 1.1402(a)-2 ; (9) Characterized by Deference to Treasury/IRS Guidance in Prop. Reg. 1.1402(a)-18 ; (10) Characterized by Deference to Treasury/IRS Guidance Under Other Code Provisions; and (11) Special Rules for LLC Members. See Part 1, pages 317-332.
6. References herein to a partner’s allocable share of partnership income generally include the allocable share of partnership losses as well, unless the context clearly requires the contrary.
7. See Letter from Patricia A. Thompson, Chair, AICPA Tax Division, transmitting “AICPA Tax Division Comments on the 2011-2012 Guidance Priority List (Notice 2011-39), June 1, 2011,” reprinted at “AICPA Responds to Request for Guidance Priority List Topics,” 2011 TNT 107-24 (6/1/11).
8. The remaining 1% interest is not accounted for in the opinion or briefs, and may be a rounding error.
9. There is no indication in the opinion that the taxpayer provided evidence that the LLP interests were designated “limited partnership interests” in the law firm’s organizational documents, or any discussion by the court as to the effect, if any, that such a designation would have on its analysis.
10. Under this approach, the characterization of the LLE member for state law purposes as a general or limited partner would control for federal tax purposes. See Part 1, pages 317-18.
11. Respondent’s Opening Brief, pages 7, 12, and 29.
12. The IRS in footnote 11 of its Answering Brief said that because Prop. Reg. 1.1402(a)-2 was only in proposed form, the Service was *not* relying on the Regulations. The IRS merely “wanted to clarify petitioner’s reading of the proposed regulations.”
13. The court added at footnote 8, “We are mindful that at the time of the statute’s enactment, the Revised Uniform Limited Partnership Act of 1976 [section 303(a)] provided that a ‘limited partner’ would lose his limited liability protection if: ‘in addition to the exercise of his rights and powers as a limited partner, he takes part in the control of the business. However, if the limited partner’s participation in the control of the business is *not* substantially the same as the exercise of the powers of a general partner, he is liable *only* to persons who transact business with the limited partnership with actual knowledge of his participation in control.’” (Emphasis added.)

*Query* what the court was being “mindful” of: Was it “mindful” that the original dichotomy between passive/investor limited partners and active/service-providing general partners did not exist in 1977 (when Section 1402(a)(13) was originally enacted, as discussed in the text, below) and certainly does not now, with the further evolution of LLEs? Was the court “mindful” that, given the evolution of LLEs, it should not rely on state law labels (the State Law Characterization Approach)? Or was the court obscurely referring to something else altogether?
14. The court did not mention that in 1994 Treasury had issued Prop. Reg. 1.1402(a)-18 to deal with this issue, but the resulting criticism from commentators caused it to be withdrawn. Your author pointed out that under Prop. Reg. 1.1402(a)-18 the lawyers of a law firm could contend, in certain circumstances, that they were not subject to SE tax—presumably an unintended result. See Shop Talk, “Are Lawyers in LLCs Exempt From Self-Employment Taxes?,” 82 JTAX 190 (March 1995), and Shop Talk, “Are Retirement Payments to Limited Partners and LLC Members Subject to Self-Employment Tax?,” 86 JTAX 62 (January 1997).
15. TRA ’97, section 935. The Tax Court also quoted verbatim a “Sense of the Senate” resolution with respect to Prop. Reg. 1.1402(a)-2, which called on Treasury and the IRS to withdraw the Proposed Regulation and that “Congress, not [Treasury or the IRS], should determine the tax law governing self-employment for limited partners.” 143 Cong. Rec. 13297 (1997).

16. Citing *Burlington N. R.R. v. Okla. Tax Comm.*, 481 US 454, 95 L Ed 2d 404 (1987) (emphasis added).
17. H. Rep't 95-702 (Part 1), 95th Cong., 1st Sess. 11 (1997); emphasis by the Tax Court.
18. The implication is that the court will look to the legislative history for the definition or illustration of the meaning of "limited partner." There is none in the legislative history.
19. See Part 1, pages 326-28.
20. *Id.*, pages 318-326.
21. In some aspects the respective briefs urge the court to follow the Tax Court's analysis in *Garnett*, 132 TC 368 (2009), under Section 469 and Temp. Reg. 1.469-5T(e); in other regards the briefs attempt (with explanations) to distinguish the analysis under *Garnett*, Section 469, and the Temporary Regulations.
22. These are the taxpayer's arguments on brief that are founded upon Section 469, and Regulations and case law thereunder; their inclusion here should not be taken to mean that your author necessarily agrees with any or all of the listed arguments. Arguments (a)-(d) were made in Petitioner's Opening Brief; Arguments (a) and (e)-(f) were raised in Petitioner's Answering Brief.
23. The Temporary Regulation is not itself a statutory exception, of course. The Petitioner's Brief presumably meant to say "without the existence of a statutory exception, as provided in Section 469(h)(2) and elaborated on in Temp. Reg. 1.469-5T(e)(3)(ii) ...."
24. The inclusion here of the Service's arguments on brief that are founded on Section 469 and the Regulations and case law thereunder should not be taken to mean that your author necessarily agrees with any or all of the listed arguments. Argument (a) was made in the Government's Opening Brief; Argument (b) was raised in the Government's Answering Brief.
25. As stated earlier, the court found itself "left to interpret [Section 1402(a)(13)] without elaboration." See the text following note 15, *supra*.
26. See paragraphs 13 and 15 of "The Tax Court's Analysis" in the text, above.
27. See note 5, *supra*, items (2)(a) through 2(g), and Part 1, pages 319-325.
28. See Part 1, page 321.
29. 2010 Instructions for Form 1065, U.S. Return of Partnership Income, General Instructions, Definitions, General Partner and Limited Partner, page 2. The same definitions have been included in the Instructions for prior years' Forms 1065. The 2011 Instructions for Form 1065 no longer include the last-quoted sentence, perhaps in recognition of the contrary positions taken in case law and Prop. Reg. 1.469-5(e) (REG-109369-10, 11/25/11; see Part 1, page 320). The Proposed Regulation will be discussed further, in the text below.
30. Under this approach, the taxpayer and IRS (and, if they do not agree, the courts) would need to divine the legislative intent of the operative Code or Regulation provision that contains the "limited partner" or "general partner" reference, and then determine whether the LLE member should be treated as a "limited partner" or "general partner" for purposes of that operative provision. See Part 1, page 326.
31. Trivedi, "Renkemeyer Facts Limit Decision's Scope, Practitioners Say," 2011 TNT 206-6 (10/25/11) (the "Renkemeyer Limited Scope Article") (reported comments of Janine Cook, Deputy Division Counsel/Associate Chief Counsel, IRS Tax-Exempt and Government Entities Division, at Employment Taxes Committee session, ABA Section of Taxation meeting in Denver, 10/21/11).
32. See Reg. 1.1402(a)-2(d).
33. See generally Banoff, "1, 61, 83, Pay Me With Your E-qui-ty: Tax Problems Facing Service Firms (and Their Partners) Who Receive Stock or Options in Lieu of Cash Fees," 79 Taxes 29 (March 2001).
34. Stiglitz and Arking, "Renkemeyer Case Sheds Light on Law Firm Tax Issues," 17 Law Firm Partnership & Benefits Report No. 5 (July 2011), page 1.
35. For this purpose, an individual's distributive share of such income or loss of a partnership is to be determined as provided in Section 704, subject to the special rules set forth in Section 1402(a) and in Regs. 1.1402(a)-1 through 1.1402(a)-17, inclusive, and to the exclusions provided in Section 1402(c) and Regs. 1.1402(c)-2 through 1.1402(c)-7, inclusive; see Reg. 1.1402(a)-2(d). (Although Reg. 1.1402(a)-2 predates and does not reflect P.L. 95-216 (12/20/77), which inserted the special statutory rule for the determination of a limited partner's NEFSE by adding what is now Section 1402(a)(13), there has been no material change to the long-standing general rule that except as otherwise provided in Section 1402(a), an individual's NEFSE includes his distributive share (whether or not distributed) of income or loss described in Section 702(a)(8) from any trade or business carried on by each partnership of which the individual is a partner. Also see Prop. Regs. 1.1402(a)-2(d) and (g).)
36. For other purposes, the Service may combine a member's general and limited partner interests, e.g., the computation of tax basis. See, e.g., Banoff, "New IRS Rulings Expand Opportunities When One is Both a General and Limited Partner," 60 JTAX 366 (June 1984).

37. If a state law limited partnership created a “General Partner Capital Interest” and a “Limited Partner Service Interest,” there is uncertainty as to whether and how the labels would control for purposes of Section 1402(a)(13).
38. The tax consequences to the member receiving Capital Interests and Service Interests in exchange for capital and services to the partnership are beyond the scope of this article. IRS officials have informally stated that capital and profits interest bifurcation would be applied in appropriate cases so as to treat the receipt of a partnership’s profits interests for services as being governed by Rev. Proc. 93-27, 1993-2 CB 343, and Rev. Proc. 2001-43, 2001-2 CB 191. See Shop Talk, “Update on Unvested Partnership Profits Interests and Rev. Proc. 2001-43,” 95 JTAX 315 (November 2001).
39. Prop. Reg. 1.1402(a)-2(h)(3).
40. See, e.g., Elliott, “Taxpayers Can Rely on Limited Partner Employment Tax Regs, IRS Official Says,” 2010 TNT 10-2 (1/15/10) (quoting comments of Diana Miosi, Special Counsel, IRS Office of Associate Chief Counsel (Passthroughs & Special Industries), made at a District of Columbia Bar Association program); Trivedi, “After Renkemeyer, Passthroughs Can Still Rely Safely on Proposed Regs, Official Says,” 2011 TNT 89-5 (5/9/11) (the “Passthroughs Reliance Article”) (reporting Miosi’s comment at the Partnerships and LLCs Committee session of the ABA Section of Taxation meeting in Washington on 5/6/11 that, as the Proposed Regulations have yet to be withdrawn or finalized, taxpayers should rely on those Regulations); Elliott, “Practitioners Are Concerned by Trade or Business Finding in Dages,” 2011 TNT 145-3 (7/28/11), 132 Tax Notes 487 (8/1/11) (the “Concerned Practitioners Article”).
41. See, e.g., Sowell and Harvey, “Carried Interest Legislation: Out of Sight, But Not Out of Mind,” 63 U.S.C. Inst. on Fed. Tax’n—Major Tax Planning (2011); Note, “Taxing Partnership Profits Interests: The Carried Interest Problem,” 124 Harv. L. Rev. 1773 (2011).
42. See text accompanying and following note 73, *infra*.
43. See note 15, *supra*.
44. See Elliott, “Renkemeyer Rationale Consistent With Statute, IRS Official Says,” 2011 TNT 102-3 (5/26/11) (reporting remarks of Curtis Wilson at the Practising Law Institute seminar on Tax Planning for Domestic and Foreign Partnerships, LLCs, Joint Ventures and Other Strategic Alliances,” 5/25/11 in New York City (the “Renkemeyer Rationale Article”).
45. *Id.* (remarks attributed to William O’Shea, Director of the Passthroughs Group in Deloitte Tax LLP’s National Tax Office and former IRS Associate Chief Counsel (Passthroughs & Special Industries)).
46. See Elliott, “Tax Court Decision Could Reignite Debate Over Partnerships and Employment Taxes,” 2011 TNT 48-3 (3/11/11) (remarks attributed to Robert R. Keatinge) (the “Reignite Debate Article”). Keatinge reportedly stated that before Renkemeyer, most practitioners believed that the net earnings of bona fide limited partners of law firms and other professional organizations organized as state law limited partnerships in states that permit such arrangements for professional organizations (such as Colorado and Connecticut) are not subject to SE tax on their distributive share of income under Section 1402(a)(13). He observed that although Renkemeyer deals with partners in an LLP rather than a limited partnership, the judge’s reasoning in the case might be read to hold that the term “limited partner” does not necessarily include all limited partners in a state law limited partnership.  
  
Sowell reportedly views the Tax Court as really going off on “What’s the purpose of the [SE] tax?” He stated that Renkemeyer raises concerns for those who are limited partners under state law, under statutes where a limited partner can participate in the partnership’s business (without loss of limited liability). See the Renkemeyer Limited Scope Article, *supra* note 31 (comments attributed to James B. Sowell).
47. See, e.g. Johnson, TC Memo 1990-461, PH TCM ¶90461 ; Norwood, TC Memo 2000-84, RIA TC Memo ¶2000-084 ; Gamma Farms, 66 AFTR 2d 90-5252 (DC Calif., 1990), *rev’d by unpubl’d opn.* 956 F2d 1166 (CA-9, 1992). See Part 1, page 317.
48. Johnson, *supra* note 47; Norwood, *supra* note 47; Perry, TC Memo 1994-215, RIA TC Memo ¶94215 (“[s]tate law requires that certain formalities be observed to create a limited partnership,” in order for one to be a limited partner under Section 1402(a)(13) ).
49. Comments of James B. Sowell, reported in the Renkemeyer Limited Scope Article, *supra* note 31.
50. See Johnson and Norwood, both *supra* note 47.
51. See Gamma Farms, *supra* note 47.
52. Jackel, “Has Politics Trumped Policy?,” 2011 TNT 94-8, 131 Tax Notes 745 (5/16/11).
53. *Jacobellis v. Ohio*, 378 U.S. 184 (1964) (Stewart, J., concurring).
54. Citing 1 *Bromberg and Ribstein on Partnership* (Aspen, 2002-2 Supp.), §1.01(b)(3).
55. Footnote 8 of the opinion quotes from section 303(a) of the 1976 revision of the Uniform Limited Partnership Act, which focuses on the consequences of a limited partner’s taking part in the *control* of the business, which is not the same as engaging in the business operations of the partnership.
56. Former Section 512(b)(13)(C). In addition, under former Section 512(b)(13)(B), the interest had to be in a limited partnership formed in a state whose limited partnership act corresponded to ULPA (1916) section 7, i.e., “under which a limited partner has no right to take part in the control of the business without becoming liable as a general partner.”

As background, an otherwise tax-exempt organization is subject to tax on its UBI, which is income derived from a trade or business regularly carried on, “the conduct of which is not substantially relative” to the exempt functions of the organization. See Sections 512(a) and 513(a). Ordinarily, an exempt organization that is a partner (limited or general) in a business venture reported as UBI its share in the gross income of the partnership, less deductions directly connected therewith. See Section 512(c) ; Rev. Rul. 79-222, 1979-2 CB 236. An exception to this rule was provided in former Section 512(b)(13), so that receipts of a charitable, scientific, educational or similar trust, if from a limited partnership interest, could be excluded from taxation.

57. S. Rep’t No. 1402, 85th Cong., 2d Sess. (1958).
58. Banoff, “Tax Distinctions Between Limited and General Partners: An Operational Approach,” 35 Tax L. Rev. 1 (1979) (the “Tax Distinctions Article”), pages 75-76.
59. See Shop Talk, “Tax Consequences of Service Partnerships’ Investment Programs,” 100 JTAX 379 (June 2004).
60. Elliott, the Reignite Debate Article, *supra* note 46 (remarks attributed to Robert G. Honigman).
61. Cohen, “Real Estate Professionals Under Code Sec. 469; PIP and ‘Limited Partners’ for Self-Employment Tax,” J. Passthrough Entities (May-June 2011), page 73. Cohen concludes that under the Tax Court’s two-prong test, liability aspects and authority aspects are of no importance, “which (if correct) would mean that, in the extreme, partners in a general partnership could actually be ‘limited partners’ under Section 1402(a)(13) so long as they do not participate and their interest in the partnership is merely an investment.” Although Cohen concludes “this is probably taking the analysis of the Tax Court too far,” neither he nor we see anything in Renkemeyer that would limit the application of the two-prong test to solely tax partnerships that are not state law general partnerships, i.e., to LLEs whose members have limited liability protection. Indeed, as stated above, the presence of limited liability is disregarded by the court in defining who is a “limited partner”; why assume it would matter to this court that the partner with a “mere investment” who does not actively participate in the partnership’s business operations is a member of a state law *general* partnership?
62. Elliott, the Reignite Debate Article, *supra* note 46 (reported comments of Claire Y. Nash, Assistant Professor of Accounting, Florida Atlantic University).
63. Koski, “Partners of Law Firm Organized as LLP Held Liable for Self-Employment Tax on Distributive Share of Earnings—Uncertainty on How SE Tax Applies to LLPs and LLCs Remains,” 89 Taxes No. 8 (August 2011), page 37.
64. *Id.* Also see Shop Talk, “What is Legal Effect of Proposed Regs.?,” 69 JTAX 279 (October 1988). See generally Part 1, pages 328-29.
65. Koski, *supra* note 63.
66. See note 40, *supra*.
67. The reference in Garnett to Prop. Reg. 1.1402(a)-2(h) occurred merely in connection with an attempted definition of “limited partner” intended to be given limited scope (i.e., solely for purposes of Section 1402(a)(13), and not Section 469(h), or Temp. Reg. 1.469-5T(e)(3), which were at issue in Garnett).
68. As to a member of a service partnership who provides both capital and services to the partnership, see paragraph 5 in the text, below.
69. See “Unanswered Questions,” number 6.
70. See generally Shop Talk, “Are Retirement Payments to Limited Partners and LLC Members Subject to Self-Employment Tax?,” *supra* note 14.
71. For example, if attorney Renkemeyer was a 33% profit share partner who was disabled for six months in the LLP’s current year, the disability payment would be to provide him with 33% of the profits for the six months he is disabled.
72. See discussion in the text accompanying note 34, *supra*.
73. See the Passthroughs Reliance Article, *supra* note 40 (reported comment attributed to Diana Miosi that although Renkemeyer was decided in the context of an LLP, the IRS believes the opinion strongly supports the notion that a service partner cannot be excluded [from NEFSE]. The article then quotes Miosi as saying, “That’s clearly on the Service’s mind. ... There’s been no final decision on what we’re going to do with respect to LLC’s, but the opinion is there, and it can be read by everyone”).
74. See “Unanswered Questions,” number 5, in the text accompanying notes 44-58, *supra*.
75. See, e.g., the Johnson, Norwood, and Gamma Farms cases, all cited in note 47, *supra*.
76. See Part 1, pages 317-318.
77. See Part 1, pages 326-327.
78. “Seeing law firm partners trying to assert that they’re not subject to self-employment taxes seems ridiculous” (comment of Audrey Ellis, director, PricewaterhouseCoopers LLP, at an Employment Taxes Committee panel, during an ABA Section of Taxation meeting on 10/21/11, reported in the Renkemeyer Limited Scope Article, *supra* note 31).
79. Sullivan, “Economic Analysis: Renkemeyer Annual Cost to Partners Could Exceed \$1 Billion,” 2011 TNT 55-2 (3/22/11).

80. The Concerned Practitioners Article, *supra* note 40 (reporting on the N.Y. State Bar Association Summer Meeting).
81. See the Renkemeyer Rationale Article, *supra* note 44 (remarks attributed to William O'Shea, former IRS Associate Chief Counsel (Passthroughs & Special Industries)).
82. Elliott, the Reignite Debate Article, *supra* note 46.
83. See Sullivan, *supra* note 79.
84. Kehoe et al., "Renkemeyer Article Rankles Attorneys, Accountants," 2011 TNT 74-9 (4/18/11) (a group of attorneys and accountants who prepare law firm and law firm partners' returns report that "[n]one of us was aware of one single case where a law firm or its partners are treating their income from practicing law as not subject to self-employment tax").
85. See, e.g., Elliott, the Reignite Debate Article, *supra* note 46 ("... if Renkemeyer has done anything, it has only increased the uncertainty").
86. See "Unanswered Questions Under 1402(a)(13) After *Renkemeyer*," in the text, above.
87. See, e.g., comments of Messrs. Wilson, O'Shea, and Keatinge, in the text accompanying notes 44-46, *supra*, and Cohen, note 61, *supra*.
88. See, e.g., the Renkemeyer Limited Scope Article, *supra* note 31.
89. The taxpayer expressly contended that the attorney-partners were "limited partners" for purposes of Section 1402(a)(13) because they were members of an LLP.
90. See the Tax Distinctions Article, *supra* note 58.
91. ABA Section of Taxation, Task Force on Limited Liability Companies. See "ABA Comments on Treatment of LLC Members as General or Limited Partners," 96 TNT 232-15. See also Part 1, fn. 46.
92. Elliott, the Reignite Debate Article, *supra* note 46 (statements attributed to Robert G. Honigman, formerly employed in IRS Office of Associate Chief Counsel (Passthroughs & Special Industries)).
93. *Id.* (reporting on comments by Jodi J. Schwartz, Esq.).
94. See AICPA 2011-12 Guidance Priority List, note 7 *supra* and accompanying text. The report of the AICPA Tax Committee's Partnership Taxation Technical Resource Panel (Sarah I. Staudenraus, Chair) ranked the following the second highest of 17 partnership taxation projects recommended for inclusion on the 2011-2012 Guidance Priority List: "2. Guidance is needed on the treatment of limited liability company members (and limited partners in light of recent judicial rulings [Author Note: read "Renkemeyer"]) under section 1402(a)(13). Regardless of the political nature of this issue, some taxpayers aggressively avoid classifying LLC income as earnings from self-employment, while others may be overly conservative in this regard. Without guidance, widespread inconsistency will continue to flourish and practitioners trying to do the 'right' thing have difficulty retaining clients who prefer an overly aggressive position. The Service should withdraw and re-propose or finalize existing regulations addressing this important issue."
95. Office of Tax Policy and IRS 2011-12 Priority Guidance Plan (updated as of 8/19/11, released 9/2/11). Nevertheless, the issuance of "Regulations under Section 469(h)(2) concerning limited partners and material participation" made the Priority Guidance list for 2011-12, as expected.
96. *Id.*
97. The devil is in the details of the "right to manage" standard as formulated in Prop. Reg. 1.469-5(e). Whether that standard is ultimately retained, and if it is, whether it can be promptly refined in response to bar associations' and practitioners' comments and criticism, is to be determined.
98. Prop. Reg. 1.892-5(d)(iii)(B) (REG-148537-06, 11/2/11).
99. The Tax Distinctions Article, *supra* note 58.
100. See "Potential 1402(a)(13) Impact on Members of Various Types of LLEs," in the text above.
101. Mayo Foundation for Medical Education and Research, 107 AFTR 2d 2011-341, 178 L Ed 2d 588 (2011). See Lipton and Young, "Mayo Foundation, Treasury Regulations, and the 'Death' of *National Muffler*," 114 JTAX 206 (April 2011); Lipton and Young, "Courts Split on Validity of Section 6501(e)(1)(A) Regulations After *Mayo Foundation*," 115 JTAX 21 (July 2011).
102. See Part 1, pages 320-21.
103. ABA Section of Taxation, "Comments on Proposed Regulations Issued Under Section 469," reprinted in "ABA Tax Section Offers Comments on Proposed Material Participation Regs," 2012 TNT 88-63 (5/4/12); New York State Bar Association Tax Section, Report 1259, "Report on Proposed Regulations Under Section 469 Governing the Definition of Limited Partner" (2/29/12), reprinted in "NYSBA Tax Section Suggests Changes to Proposed Material Participation Regs," 2012 TNT 41-11 (2/29/12). Technical problems with Prop. Reg. 1.469-5(e)(3) already have been brought to Treasury's attention. See, e.g., Elliott, "IRS Might Clarify Limited Partner Interest Test," 3 Tax Notes 280 (2012).



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In addition to his work on behalf of the firm's clients, Mr. Banoff is also a nationally and internationally known author and lecturer. Editor of the *Journal of Taxation's* monthly "Shop Talk" column since 1985, he has also written over 200 leading articles in the tax area. He is co-author of two books: "Illinois Limited Liability Company - Forms and Practice Manual" (Data Trace Legal Publishing Inc. 2009) and "Limited Liability Companies and S Corporations" (Illinois Institute of Continuing Legal Education 2010). Also, Mr. Banoff has been a Lecturer in Law at the University of Chicago Law School, where he taught an Advanced Seminar on Real Estate Transactions with emphasis on choice of form of entity, fiduciary duties, economic analysis of investments and taxation matters. He also serves on the Law School's Annual Tax Conference Planning Committee (which he chaired in 1993 and 1994).

A past chairman of the Chicago Bar Association's Federal Taxation Committee, he now serves on its Executive Council. He is actively involved in the American Bar Association Section of Taxation, and is a frequent program speaker on partnership, limited liability company and tax planning matters. Actively involved in executive compensation and professional firm organization and management matters, Mr. Banoff is past Chairman of the Chicago Bar Association's Large Law Firm Committee and counsels law and accounting firms on various tax and non-tax matters.

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