# Using Partnerships in Corporate Transactions

by Robert W. Wood • San Francisco

Although the topic was discussed with some vigor a few years ago, one hears relatively little at this time about those complex transactions that integrate the partnership tax rules with the corporate tax rules. There is little doubt that the IRS is concerned with abusive (or at least IRS considers them abusive) partnership transactions, in which what might be a taxable sale at the corporate level would be avoided.

Consider the recent issuance of Technical Advice Memorandum 9822002. There, the IRS ruled that a partner's exchange of its operating business for a partnership interest plus cash and stock contributed to the partnership by a corporate partner should be treated as a sale between the partnership and the partner. The ruling goes on to conclude that the partnership should be treated as an aggregate of its partners (rather than as an entity) for purposes of applying Section 1032.

There has, of course, been fundamental debate about whether an entity or aggregate approach to partnership taxation is more appropriate, particularly in the corporate context. Under the entity theory, a partnership is treated as a separate taxpayer having at least some entity identity and characteristics. The aggregate theory of partnership taxation suggests that the partnership is merely a collection of partners (who, after all, will pay tax based on their respective interests as shown on their Forms K-1).

The aggregate vs. entity question has been present in a variety of contexts. Even the recently issued continuity of interest regulations (on this topic, see Willens, "Accounting's Pooling Rules and Tax-free Reorganization Rules Coalesce," this issue, p. 1). Even these recently issued regulations reflect a somewhat schizophrenic attitude about this age-old issue, adopting both the aggregate and the entity approaches in dealing with transfers to partnerships. (See "Guidance Sparse on Use of Partnerships in Corporate Transactions," *Tax Notes*, June 15, 1998, p. 1400.)

### Further Word?

The IRS seems not to want to bring these issues up for serious discussion, and has missed at least one recent opportunity to speak publicly about the issue (*Id.*). However, private letter rulings do come along. In addition to Technical Advise Memorandum 9822002 mentioned above, the Service recently issued Letter Ruling 9822037. There, a parent corporation caused its subsidiary to merge into the parent's recently formed single-member LLC. The LLC was the survivor. The IRS ruled that this transaction qualified as a Section 332(a) liquidation.

Even though an LLC is typically treated as a partnership, the fact that this was a single-member LLC presumably resulted in that entity being treated as a corporation for these purposes. That does suggest (although there may be reasons not to do this in particular cases) that an existing partnership or LLC might be pared down of most of its partners in order to comply with this rather slick one member rule.

Ultimately, it may be some time before these partnership techniques (particularly with regard to affiliated group transactions) has been fully explored. In the meantime, advisors will likely still be scribbling diagrams to try to mechanically work through what are often difficult theoretical problems. ■