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IRS and Treasury Issue Proposed Regulations on Partnership Transfers

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WASHINGTON — The Treasury Department and the Internal Revenue Service today issued proposed regulations providing guidance for determining when a transfer of consideration to a partnership by a partner and a transfer of consideration from that partnership to a different partner constitute a disguised sale of a partnership interest.

These proposed regulations are intended to provide guidance regarding disguised sales of partnership interests. Generally, the proposed regulations follow the model provided in the existing regulations under § 707 governing disguised sales of property between partners and partnerships. In particular, the proposed regulations provide, generally, that where a transfer of consideration to partner A by a partnership would not have happened "but for" the transfer of consideration to the partnership by partner B, the transfers are treated as a sale of all or a portion of partner A's interest in the partnership to partner B for all purposes under the Internal Revenue Code. Where the transfers to and from the partnership do not occur on the same date, the transfers are treated as a sale only if the later transfer is not dependent on the entrepreneurial risks of partnership operations. The proposed regulations provide that these determinations are made based on all of the facts and circumstances.

"These proposed rules benefit both the taxpaying community and the Internal Revenue Service," said IRS Chief Counsel Don Korb. "The rules provide taxpayers and tax practitioners with guidance on how to structure partnership contributions and distributions without getting caught up in the disguised sale rules. They also provide for a longer disclosure period that will facilitate the examination of questionable transactions involving partnerships."

The proposed regulations incorporate the timing presumptions of the existing regulations under § 707, but also provide additional presumptions and exceptions for transactions that are unlikely to constitute disguised sales of partnership interests. The proposed regulations include detailed rules for determining what constitutes a transfer of consideration, including whether and to what extent the shifting or assumption of liabilities, including partnership liabilities, among partners and the partnership constitutes a transfer of consideration. An anti-abuse rule is also provided.

In response to a recommendation of the Joint Committee on Taxation in its *Report of Investigation of Enron Corporation and Related Entities Regarding Federal Tax and Compensation Issues, and Policy Recommendations* (February 2003), the regulations generally would extend the existing disclosure requirement for disguised sales of property from two years to seven years. The same disclosure requirement would be incorporated for disguised sales of partnership interests.

The preamble to the proposed regulations states that the Treasury Department and the Internal Revenue Service also plan to review the existing regulations under §707 for deficiencies and technical ambiguities and to amend those regulations as necessary before these proposed regulations are issued as final regulations.

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