



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
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OFFICE OF  
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR Area Counsel(Heavy Manufacturing, Construction and  
Transportation), Washington, D.C.

FROM: BLAISE DUSENBERRY , Assistant Branch Chief,  
Branch 3, Administrative Provisions and Judicial Practice  
CC:PA:APJP:Br03

SUBJECT: Small Partnership Exception- Tax Exempt Entity Treated as  
"C Corporation" partner

This Chief Counsel Advice responds to your memorandum dated April 10, 2001. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Partnership =  
Y =  
A =  
B =

ISSUES

Is the partnership's Y year Federal income tax return subject to the audit procedures of I.R.C. § 6221 through 6234 ("TEFRA") or is the partnership exempt from those procedures under the "small partnership exception" to the TEFRA rules?

CONCLUSIONS

Since both corporate partners qualify as "C corporations" within the meaning of sections 6231(a)(1) and 1361(a)(2), the partnership is a "small partnership" excepted from the TEFRA audit procedures.

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## FACTS

The taxpayer is a limited partnership. Since its inception, the Partnership has had two partners: A, the sole general partner, and B, the sole limited partner.

A is an incorporated entity which files with the Internal Revenue Service as a C corporation of a Form 1120. B is an exempt organization under the Federal income tax laws. For its tax year Y, B filed an information return (Form 990). B was chartered as a corporation and has never elected to be taxed as an S corporation.

For year Y the Schedule K-1 for the Partnership's general partner lists A as a "corporation." In contrast, the Schedule K-1 for the limited partner designates B as "tax exempt," without including the words "Inc." or "Co." after B's name. Although A is designated as the tax matters partner on the Partnership's Form 1065, the Partnership indicated that it is not subject to the TEFRA procedures. While the Analysis of Net Income (Loss) on page 4 of the Form 1065 identifies both A and B as "Corporate," the Form 1065 for the following year identifies B as an "Exempt organization."

## LAW AND ANALYSIS

The Partnership asserts that, under the "small partnership exception" set forth in I.R.C. § 6231(a)(1)(B), it is not subject to the TEFRA procedures for year Y. For tax years ending after August 5, 1997, I.R.C. § 6231(a)(1)(B) provides that the term "partnership" shall not include any partnership if such partnership has ten or fewer partners each of whom is an individual (other than a nonresident alien), a C corporation, or an estate of a deceased partner. That the Partnership has ten or few partners is clear. However, the dispute concerns whether the limited partner, an exempt organization, should be characterized as a C corporation for purposes of the small partnership exception.

As support for its position, the taxpayer points to I.R.C. § 1361(a)(2). That section provides that, "[f]or purposes of this title, the term 'C corporation' means, with respect to any taxable year, a corporation which is not an S corporation for such year." The taxpayer argues that, for purposes of this exception, B constitutes a C corporation because it is incorporated and files information returns as a corporation. Therefore, the taxpayer maintains, the Partnership is exempt from the TEFRA rules.

Section 1361(a)(2) explicitly defines a corporation that is not an S corporation as a C corporation "for purposes of this title" referring to Title 26 (the Internal Revenue Code). The TEFRA provisions fall within Title 26. Thus, a tax exempt corporation is a "C corporation" for the purposes of the small partnership exception.

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CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS



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Please call if you have any further questions.