

INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

July 2, 1999

Index (UIL) No.: 2503.03-00
CASE MIS No.: TAM-122512-98
Number: **199944003**
Release Date: 11/5/1999
District Director

CC:DOM:P&SI:B7

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No:
Years Involved:
Date of Conference:

LEGEND:

| | |
|----------|---|
| Taxpayer | = |
| Spouse | = |
| <u>a</u> | = |
| <u>b</u> | = |
| <u>c</u> | = |
| <u>d</u> | = |
| <u>e</u> | = |
| <u>f</u> | = |
| <u>g</u> | = |
| <u>h</u> | = |
| State | = |

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ISSUE:

Whether Taxpayer's transfer of limited partnership interests to Taxpayer's children constitute gifts of present interests for purposes of § 2503(b) of the Internal Revenue Code.

CONCLUSION:

The gifts of limited partnership interests by Taxpayer constitute gifts of present interests that will qualify for the annual exclusion under § 2503(b). This Technical Advice Memorandum does not address issues relating to the valuation of the gifts nor does it consider the application of § 2704 to the restrictions contained in the Partnership Agreement.

FACTS:

Taxpayer and Spouse created a family limited partnership in a. Taxpayer and Spouse each own a b percent general partnership interest. Taxpayer also owns a c percent limited partnership interest and Spouse owns a d percent limited partnership interest.

In e, Taxpayer gifted an f percent limited partnership interest to each of Taxpayer's g children, respectively, for a total gift of h percent. Each percent of limited partnership interest equals one unit of limited partnership interest.

Article 6.1 of the Partnership Agreement provides that the net cash flow may or may not be distributed at least annually to the partners in accordance with their respective percentage interests. The timing and amount of any distributions shall be within the sole discretion of the general partners.

Article 8.1(a) of the Partnership Agreement provides that, subject to the requirements in Article 8, a limited partner shall have the right to assign a partnership interest only by written assignment, the terms of which are not in contravention of any of the provisions of this Agreement, which assignment has been duly executed by the assignor and assignee, received by the partnership and recorded on the books of the partnership.

Article 8.1(b) of the Partnership Agreement provides that anything in the Agreement to the contrary notwithstanding, both the partnership and the general partners shall be entitled to treat the assignor of a limited partner's partnership interest as the absolute owner thereof in all respects, and shall incur no liability for distributions of cash or other property made in good faith to the assignor, until such time as the written assignment has been received by the partnership and promptly recorded on the

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books of the partnership unless the general partners reasonably believe the assignment to be illegal, void, or otherwise not in compliance with the terms of this Agreement.

Article 8.1(c) of the Partnership Agreement provides that an assignee of a limited partner shall be entitled to receive the distributions of net cash flow or other property from the partnership and the allocation of partnership profits, losses, and credits (including all items thereof) attributable to the interest acquired by reason of such assignment which are distributed or allocated, as the case may be, from and after the effective date of the assignment of such interest to it, except as provided in Section 8.1(b) of this Article.

Article 8.2(a) of the Partnership Agreement provides that no assignee shall have the right to become a substituted limited partner (as defined in Section 8.3 of this Article) except upon unanimous written consent of the general partners, the granting or denying of which shall be, notwithstanding the provisions of Article 9.5(a)(6) of this Agreement, within the general partners' sole and absolute discretion and subject to whatever conditions, if any, the general partners require.

Article 8.2(b) of the Partnership Agreement provides that notwithstanding the aforementioned consent by the general partners, the admission of any assignee as a substituted limited partner shall be further conditioned as follows:

(1) The assignment instrument and such other instruments as the general partners may deem necessary or desirable to effect the admission of the assignee as a substituted limited partner being in form and substance satisfactory to the general partners;

(2) The assignor and assignee named therein executing and acknowledging such other instrument or instruments as the general partners may deem necessary or desirable to effectuate such admission;

(3) The assignee's written acceptance and adoption of all the terms and provisions of this agreement, as the same may have been amended;

(4) Such assignee, the assignor or both paying or obligating themselves to pay all reasonable expenses connected with such admission (as determined solely by the general partners, but which the general partners shall have the right in their sole discretion to waive), including, but not limited to, the cost of the presentation, filing and publishing of any appropriate documents; and

(5) Such other conditions as the general partners may reasonably impose.

Article 8.3 of the Partnership Agreement provides that a substituted limited partner is a person admitted to all the rights and who assumes all of the obligations of a

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limited partner who has made an assignment of an interest in the partnership pursuant to section 8.2 of this Article.

Article 8.4 of the Partnership Agreement provides that an assignee who does not become a substituted limited partner has no right to receive any information or account of partnership transactions, to inspect the partnership's books, to vote on partnership matters, to request a meeting of the partnership or to exercise any of the other rights of a limited partner other than to receive the share of the cash and profits, losses, and credits (including all items thereof) or other compensation by way of income to which his or her assignor would otherwise be entitled as to the partnership interest.

Article 8.5 of the Partnership Agreement provides that no transfer or assignment of any partnership interest may be made if such transfer or assignment, together with all other transfers and assignments of partnership interests within the preceding twelve months would, in the opinion of counsel for the partnership, result in the termination of the partnership for purposes of section 708 of the Internal Revenue Code, or any comparable provision then in effect.

Article 8.7 of the Partnership Agreement provides that a limited partner shall have no right to withdraw from the partnership.

Article 9.2 of the Partnership Agreement provides that the general partners shall be solely responsible for the management of the Partnership business, with all rights and powers generally conferred by law or necessary, advisable or consistent in connection therewith. In assuming the aforementioned responsibilities, the general partners shall uphold a strict fiduciary duty toward the limited partners and the Partnership, and shall be held personally liable for any breach thereof.

LAW AND ANALYSIS:

Section 2501(a)(1) provides for the imposition of a tax on the transfer of property by gift. Section 2511 provides that the gift tax applies to a transfer by way of gift whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2503(b) provides that in the case of gifts (other than gifts of future interests in property) made to any person by the donor during the calendar year, the first \$10,000 of such gifts to such person shall not, for purposes of § 2503(a), be included in the total amount of gifts made during such year.

Section 25.2503-3(b) of the Gift Tax Regulations provides that a present interest in property is an unrestricted right to the immediate use, possession, or enjoyment of the property (such as a life estate or a term certain).

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Section 25.2503-3(a) of the regulations defines "future interests" as a legal term that includes reversions, remainders, and other interests or estates, whether vested or contingent, and whether or not supported by a particular interest or estate, which are limited to commence in use, possession, or enjoyment at some future date or time.

State law applicable in this case provides that a partner is entitled to receive distributions from a limited partnership before his withdrawal from the limited partnership and before the dissolution and closing of its affairs to the extent and at the times or upon the happening of the events specified in the partnership agreement. A limited partner may withdraw from a limited partnership at the time or upon the happening of events specified in writing in the partnership agreement.

State law further provides that except as provided in the partnership agreement, a partnership interest is assignable in whole or in part. The assignee of a partnership interest, including the assignee of a general partner, may become a limited partner if and to the extent that: (1) the assignor gives the assignee that right in accordance with authority described in the partnership agreement, or (2) all other partners consent.

Under the terms of the Partnership Agreement, the general partners are solely responsible for the management of the Partnership business. The timing and amount of any distributions are within the sole discretion of the general partners. The Partnership Agreement gives a limited partner the right to assign his or her partnership interest by written assignment. From the date of the assignment, the assignee is entitled to receive the distributions of net cash flow or other property from the partnership and the allocation of partnership profits, losses, and credits attributable to the interest.

The management powers the Taxpayer/general partner possesses under the Partnership Agreement in this case, including control over partnership distributions, are consistent with the powers granted to general partners under State law and are similar to the powers possessed by general partners in most limited partnerships. The Taxpayer possesses no powers as a general partner that are not otherwise contained in a standard limited partnership agreement. The Taxpayer/general partner's powers are different from a trustee's discretionary authority to distribute or withhold trust income or property (*i.e.*, a power that generally results in the characterization of a gift to such a trust as a gift of a future interest). See *e.g. Fondren v. Commissioner*, 324 U.S. 18 (1945), in which the Court concluded that the transfer of interests in a trust were not gifts of present interests where the trustee had the discretion to withhold trust income.

Under the Partnership Agreement, the donees/limited partners may expect the highest standard of conduct from the general partners in their management of the Partnership. More specifically, the Partnership Agreement provides that in assuming their responsibilities under the Partnership Agreement, the general partners are to

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uphold a strict fiduciary duty toward the limited partners and the Partnership, and are to be held personally liable for any breach thereof.

We believe that in this case, Taxpayer's gifts of limited partnership interests to Taxpayer's children constitute outright gifts of ownership interests in the Partnership. Each donee of a limited partnership interest received the immediate use, possession, and enjoyment of the interest, including the right to sell or assign the interest. These rights entitled the donees to any current economic benefits generated by the limited partnership interests.

Accordingly, we conclude that the gifts of limited partnership interests by Taxpayer constitute gifts of present interests that will qualify for the annual exclusion under § 2503(b).

CAVEAT(S)

A copy of this technical advice memorandum is to be given to Taxpayer. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.