PARTNERSHIP TAXATION - J.D.
LAW 6930
Spring 2011

Tues., Wed., Thurs. 10:00 A.M. Professor Martin J. McMahon, Jr.
Class Room 283 Office: Room 312F
Office hours: Mon., 3:30 - 5:00 P.M. Tel: (352) 273-0931
& by appointment e-mail: mcmahon@law.ufl.edu

SYLLABUS

Required Texts

(1) McDaniel, McMahon and Simmons, Federal Income Taxation of Partnerships and S Corporations, 5th Ed. (Foundation Press 2012)

(2) McDaniel, McMahon and Simmons, of Study Problems to Accompany Federal Income Taxation of Partnerships and S Corporations, 5th Ed.

(3) 2012 Edition, Selected Federal Taxation Statutes and Regulations (West)

IMPORTANT ADVICE

Learning without thinking is useless
Thinking without learning is dangerous
Confucius

COVERAGE

The primary focus of this course is the structure of Subchapter K of the Internal Revenue Code, which provides the rules governing taxation of partnerships and partners (including most limited liability companies and their members) — formation, allocations, distributions, sales of interests, and liquidations. This course will cover the relevant Code sections, the Regulations thereunder, and judicial interpretations of the Code and Regulations.

CLASS SCHEDULE

Classes meet on Tuesdays, Wednesdays, and Thursdays from 10:00 to 11:50 P.M., throughout the semester, with the following exceptions. The class scheduled for Thursday, Jan. 31 will not meet and will be rescheduled to another date.
PREPARATION AND CLASS PARTICIPATION

You are expected to be prepared every day and to participate actively in class discussion. Adequate preparation includes studying the casebook and the assigned sections of the Code and Regulations, and being prepared to discuss in class the assigned readings and any assigned problems. [Note: Your Volume of Selected Code and Regulations sections is highly edited. The real Code and Treasury Regulations are much longer, more detailed, and comprehensive and answer specifically many more questions than are dealt with in the student oriented materials you are using.] You should prepare in advance a written analysis of all Study Problems relating to the assignment, including citations to relevant authority that are coordinated to the assigned reading and any necessary calculations. I recommend that everyone join a study group within which you can compare your tentative answers to the problems and refine them. Written answers will not be collected, but without them it will be difficult to follow and participate in class discussion. We will cover as many of the problems as we can in class, but there is no guarantee that we will have the time to examine the answer to every question in detail. The level of preparation of answers to the problems determines the extent to which we have time to examine them in class. Although we will not directly cover all aspects of every problem in class discussion, advance preparation of these problems is a predicate to understanding the concepts that will be discussed in class. It is my practice randomly to call on students to answer questions as well as to accept volunteer answers. **Always bring your Code and Regulations volume to class** along with your casebook and study problems.

ATTENDANCE

Regular attendance at classes is required. You are expected to arrive on time for class and to remain seated for the entire class. To be counted as attending class, you must be in the room for the entire class. Please e-mail me to request an excused absence or to explain an absence. Recognized religious holidays are automatically excused absences. Please e-mail me in advance a list of the holidays on which you will be absent for religious observances. The point score on the final examination will be reduced by 2 points (out of 100) for each unexcused absence. Any student who has more than seven unexcused absences will be excluded from the examination.

ELECTRONIC DEVICES

You may use notebook computers to access your own notes on your computer hard drive and to take note during class. No other use of a notebook computer is permitted. You may not access any programs or the internet for any purpose other than to read your notes or take notes concerning this class. That said, I strongly recommend against using computers in class. The point of the class session is to critically discuss in real time the ideas in the material, evaluate the points made by other people in the class, and solve the problems, not to record a transcript of what I or others might say. Turn off all cellular telephones during class. If you have a special reason that someone might need to contact you during class hours (e.g., pregnant spouse, ill relative), you may keep your phone on as long as the ringer is off and it is set to vibrate. Please warn me in advance that you might be receiving a call and need to leave.
QUESTIONS AND OFFICE HOURS

If you are still struggling to understand the material after the relevant class, come see me in my office. I have scheduled office hours for Mondays, from 3:30 - 5:00 P.M. In addition, I am available almost anytime on a drop-in basis or by appointment. If you want to schedule an appointment, please e-mail me. DO NOT e-mail me questions to be answered by e-mail. If you do, I will respond that you should come see me. I find it far, far more productive to discuss questions face-to-face.

EVALUATION

Grades will be assigned on the basis of a take-home final examination that will be distributed on the last day of Law School classes and which will be due on the date and at the time at which the examination is scheduled to end on the official examination schedule. The format of the examination will be problem solving essays and your response will be limited to 16 - 18 typewritten pages. The grade will be based on the demonstrated understanding of the principles of law covered in materials and in class and their application according to the course objectives section of this syllabus. Little credit will be given for merely reciting rules of law or spotting issues. Your answer must be specifically directed to the facts and the question that you have been asked and should resolve the issues and explain the legal reasoning underlying your resolution of the issues. The organization, clarity, grammar (including sentence structure), and the proper use of terms of art in your answer also affect the grade. A copy of the final examination from the Fall of 2004 is attached to give you an idea of the nature of the format and level of complexity of the questions that will be asked, as well as some idea of the level of comprehensiveness. The exact focus of the examination questions changes from year-to-year. The final examination will be graded anonymously. Grades will follow the University of Florida Grading System. See http://www.registrar.ufl.edu/catalog/policies/regulationgrades.html. The grade achieved on the examination can be raised one grade levels (e.g. from B to B+) as a result of continuous active voluntary participation in class discussion demonstrating familiarity with the assigned materials. Quality is as important as quantity. Your grade or the examination can be similarly lowered as a result of repeated poor class participation demonstrating lack of familiarity with the assigned materials. Grades also will be adjusted for unexcused absences as provided in the paragraph regarding Attendance.
COURSE OBJECTIVES

1. Learn to carefully read the Code and Regulations. Precision counts.
   a. Pay attention to each and every word and punctuation mark.
      - If you don’t understand a Code section the first time, reread it carefully, as many times as necessary, until its meaning become clear. [If you still don’t understand it after preparing and attending class, ask your instructor for help.]
   b. Recognize that most sections of the Code are either (1) definitions or (2) “if ... then ...” rules. The Code never “permits” or “prohibits” a taxpayer from engaging in any particular transaction (apart from defining specified tax crimes). The Code merely prescribes the tax results that follow from the transaction, whether or not it is legal (or civilly actionable) under state, or non-tax federal, law.
   c. Understand that some sections of the Code are so complicated that you may need to know what they purport to do before you read them. The best primary source of this information is legislative history, i.e., Congressional Committee Reports and Staff of the Joint Committee General Explanations of Tax Legislation [Bluebooks]. They are invaluable guides in interpreting the statutory language. [Your casebook and other course materials provides excerpts from the various legislative history materials for many Code sections.
   d. Learn to apply the rules precisely as expressed in the Code and Regulations, not paraphrased generalizations or short-cuts.
      - Although short-cuts and rules of thumb often produce correct answers in a majority of their applications, they also often produce incorrect answers, particularly in counter-intuitive fact patterns. For example, a rule of thumb that provides a shortcut when applying a statutory formula to a transaction involving appreciated property might not work if the property is depreciated in value.
   e. Tax law is not horseshoes. Code sections are not applied on a “close enough” principle.

2. Learn the vocabulary, i.e., “tax jargon,” and use it precisely and accurately.
   a. Rely on the terminology and words of the Code and Regulations. Do not make up your own terms of art. Even though they may help you remember a concept or a rule, your use of them will tend to confuse others or misconvey your analysis.
   b. Use the correct word in the correct context, for example, income items that are not included in gross income are “excluded,” not “deducted,” and payments that are subtracted in computing taxable income are “deducted,” not “excluded,” “realized” gain or loss is different than “recognized” gain or loss.
   c. Do not use mutually inconsistent terms simultaneously, for example, “deductible as a capital expense.”

3. Lean to apply the law to the particular facts.
   a. Understand the facts of any particular problem. Figure out what happened – e.g., who paid what to whom and why – before trying to apply the tax law.
(1) Pay attention to and consider the relevance of each and every fact. Learn to sort the relevant from irrelevant facts.

(2) Learn how to graphically depict transactions to more easily understand the nature and economics of the transaction.

b. Understand that in multi-party transactions different sections of the Code and Regulations may apply to different parties. Do not confuse the parties or the respective rules that apply to them.

c. Remember that the treatment of one party to a transaction is not always symmetrical to that of another. For example, a payee does not necessarily have exempt income merely because the payor is denied a deduction, and the buyer’s basis for property is not necessarily the exact same amount as the seller’s amount realized.

4. Learn to explain the precise reason, applying the Code, Regulations, and relevant case law and Revenue Rulings for each and every answer to each and every issue presented by any fact pattern. Remember that “public policy” considerations that are often applied in other areas of the law are less significant in resolving tax issues. For example, deductions are not generally disallowed simply because they are incurred to further an illegal activity.

5. Learn how to distinguish situations that have a single clear answer from those in which the answer is ambiguous.

a. Answer questions that have clear answers directly.

b. If a question does not have a single clearly correct answer, articulate all of the arguments for and against each possible resolution and weight them in order of the likelihood of application. In such a case attempt to ascertain the answer that is more likely than not the correct answer and be prepared to support your conclusion.

c. Don’t make frivolous arguments or make it sound like there are arguments both ways when there are not.

6. Understand that the IRS is not Darth Vader – it does not automatically take an “anti-taxpayer” position in every factual situation. The IRS does not seek to include in gross income items that clearly are excluded by the Code, Regulations, or case law, and it does not seek to disallow deductions that clearly are allowed by the Code and Regulations. Nor does the IRS take positions contrary to the Regulations, Revenue Rulings, or Supreme Court cases. It does, of course, argue the government’s side in cases where the law is unclear.

7. Learn to recognize that there may be situations in which you do not have sufficient facts to give a definitive answer, but learn not to be too hasty in concluding that you need additional facts. In such cases, ask for additional facts or provide an answer for each of the possible alternative scenarios.

8. Understand that all of the facts in their totality must be considered simultaneously to determine the correct answer or best arguments. Consider all of the relevant facts before reaching a conclusion.
9. Understand that descriptions of the facts, whether in problems or as explained by clients may use a word in its colloquial sense when the word has a different (often narrower) meaning as a legal term of art. Remember that the same word can have different meanings in different doctrinal areas of law, and that different words used in different doctrinal areas of law can be synonyms for analogous legal conclusions.

10. Learn how to integrate rules from different Code sections and Regulations sections to determine:
   a. Their interaction,
   b. Which section controls if they conflict – remember particularly that capitalization trumps deductibility, i.e., an expense described in a deduction section must nevertheless be capitalized in many instances,
   c. Whether the principles developed under one Code (or Regulations) section can be applied by analogy to interpret another section, even though the sections neither interact nor conflict.

11. Above all else: Develop the confidence to read and understand a section of the Code and Regulations that you have never seen before and to apply it properly to a fact pattern that you have never before encountered.

ASSIGNMENTS

The following assignments reflect the order of coverage. Many assignments will require more than one class session. However, unless instructed otherwise, go on to a new assignment for the next class. Even if it will take more than one day to complete an assignment, you are expected to prepare the entire assignment before the first class and to refresh your recollection for subsequent classes. ALL ASSIGNMENTS INCLUDE THOROUGH PREPARATION OF THE COORDINATED STUDY PROBLEMS. Because many of the answers involve detailed calculations, you should prepare all of your answers in writing.

<table>
<thead>
<tr>
<th>Topic</th>
<th>Assignment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Introduction</td>
<td>pp. 1 - 5</td>
</tr>
<tr>
<td>Definition of Partnership (Part 1)</td>
<td>pp. 5 - 15</td>
</tr>
<tr>
<td>2 Definition of Partnership (Part 2)</td>
<td>pp. 15 - 39</td>
</tr>
<tr>
<td>3 Receipt of Partnership Interest for Property</td>
<td>pp. 41 - 51</td>
</tr>
<tr>
<td>4 Contributions of Encumbered Property</td>
<td>pp. 51 - 56</td>
</tr>
<tr>
<td>5 Receipt of Partnership Interest for Services</td>
<td>pp. 57-68</td>
</tr>
</tbody>
</table>

6
<table>
<thead>
<tr>
<th>Chapter</th>
<th>Topic</th>
<th>Pages</th>
</tr>
</thead>
<tbody>
<tr>
<td>6</td>
<td>Transfer of Partnership Interest for Services</td>
<td>pp. 69-83</td>
</tr>
<tr>
<td>7</td>
<td>Pass-Through of Income &amp; Loss</td>
<td>pp. 84 - 102, 105-109</td>
</tr>
<tr>
<td>8</td>
<td>Introduction to Partnership Allocations</td>
<td>pp. 111 - 126, 129 -134 [omit detailed study of regs. cited on p. 125] Do only problem 1(a) - (c).</td>
</tr>
<tr>
<td>11</td>
<td>Partnership Allocations – Substantiality</td>
<td>pp. 148 - 160</td>
</tr>
<tr>
<td>12</td>
<td>Partnership Allocations Attributable to Nonrecourse Debt</td>
<td>pp. 160 - 172</td>
</tr>
<tr>
<td>13</td>
<td>Partnership Allocations Attributable to Contributed Property</td>
<td>pp. 172 - 188 [Do problems 1 &amp; 2]</td>
</tr>
<tr>
<td>14</td>
<td>Reverse § 704(c) Allocations</td>
<td>pp. 188 - 190 [Do problems 3 &amp; 4]</td>
</tr>
<tr>
<td>15</td>
<td>Partnership Allocations Where Interests Vary</td>
<td>pp. 193 - 201 (through Item 2)</td>
</tr>
<tr>
<td></td>
<td>Family Partnerships</td>
<td>pp. 201 - 204 [Independent Study]</td>
</tr>
<tr>
<td>16</td>
<td>Partnership Recourse Debt</td>
<td>pp. 205 - 218</td>
</tr>
<tr>
<td>17</td>
<td>Partnership Nonrecourse Debt</td>
<td>pp. 218 - 229</td>
</tr>
<tr>
<td>18</td>
<td>Transactions Between Partners &amp; Partnership</td>
<td>pp. 230 - 252 [omit Item 10]</td>
</tr>
<tr>
<td>19</td>
<td>Sales of Property Between Partners and the Partnership</td>
<td>pp. 253 - 266</td>
</tr>
<tr>
<td>20</td>
<td>At-Risk Rules</td>
<td>pp. 267 - 283</td>
</tr>
<tr>
<td>21</td>
<td>Passive Activity Loss Rules</td>
<td>pp. 283 - 296</td>
</tr>
<tr>
<td></td>
<td>Title</td>
<td>Pages</td>
</tr>
<tr>
<td>---</td>
<td>-------------------------------------------</td>
<td>----------------</td>
</tr>
<tr>
<td>22</td>
<td>Sale of Partnership Interests (Part 1)</td>
<td>pp. 297-306;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>321 (Item 4)</td>
</tr>
<tr>
<td>23</td>
<td>Sale of Partnership Interests (Part 2)</td>
<td>pp. 306-322</td>
</tr>
<tr>
<td>24</td>
<td>Purchase of Partnership Interest</td>
<td>pp. 323-337</td>
</tr>
<tr>
<td>25</td>
<td>Current Distributions (Part 1)</td>
<td>pp. 339-359</td>
</tr>
<tr>
<td>26</td>
<td>Current Distributions (Part 2)</td>
<td>pp. 359-368</td>
</tr>
<tr>
<td>27</td>
<td>Mixing Bowl Transactions</td>
<td>pp. 368-374</td>
</tr>
<tr>
<td>28</td>
<td>Liquidating Distributions</td>
<td>pp. 374-391</td>
</tr>
<tr>
<td>29</td>
<td>Basis Adjustments</td>
<td>pp. 391-403</td>
</tr>
<tr>
<td>30</td>
<td>Complete Liquidation of the Partnership</td>
<td>pp. 414-427</td>
</tr>
<tr>
<td>31</td>
<td>Partnership Mergers and Divisions</td>
<td>pp. 427-437</td>
</tr>
</tbody>
</table>
UNIVERSITY OF FLORIDA
COLLEGE OF LAW

PARTNERSHIP TAXATION
LAW 6616

FINAL EXAMINATION
DECEMBER 3, 2004

TAKE-HOME EXAM
DUE: 1:00 P.M., Monday, December 6, 2004.
Return to: Graduate Tax Office, Room 320.

INSTRUCTIONS

1. This is a take home examination. You must type your answers. Your answers should not exceed 16 pages (using a font no smaller than 12 point) of standard 8 ½ x 11 inch paper, double spaced with one inch margins, if you need that much. You may single space tabular computations.

2. Number your pages and put your exam number on each page of your answer; do not put your name anywhere on the answer. Staple your answer together.

3. You must return the examination answer to the Graduate Tax Office, Room 320. Unless you hand your examination personally to an administrative assistant so that your name can be checked-off on the class roll as having returned the examination, there will be no evidence that you turned in your examination in the event that it cannot be located. If your examination cannot be found, failure to check in the return of your examination raises the presumption that it was not turned in.

4. The examination consists of three questions of approximately equal weight. That does not necessarily mean that the length of the answers can or should be expected to be equal, nor does it mean that the questions are of equal complexity.

5. Because this is a take home examination little credit will be given for merely reciting rules of law or spotting issues. Your answer must be specifically directed to the facts and the question that you have been asked. Credit will be subtracted for irrelevancies. Do not repeat the facts without integrating them into analysis or restate rules of law without integrating them into analysis. If you do so, it is very likely that you will not be able to answer the questions within the page limitation.

6. Each question sets forth all the relevant facts necessary to answer the question. If you think that additional facts are necessary, make reasonable assumptions and indicate your assumptions in your answer. Be careful not to assume away the question that I have asked. Where computations are required it is important that the reasoning and statutory authority
underlying the calculations be clearly set forth. Full credit will be given only for completely correct answers, but very substantial partial credit may be given for answers that are numerically incorrect (due to an arithmetic error) but properly explain the reasoning.

(a) Unless the facts specify otherwise, all taxpayers are on the calendar year; individuals report on the cash method, partnerships report on the accrual method.
(b) All taxpayers are unrelated unless the facts indicate otherwise.
(c) All partnerships and corporations are domestic and all individuals are U.S. citizens, unless the facts indicate otherwise.
(d) If it is necessary to compute the amount of an individual’s income tax liability to answer a question, assume that the individual is in the highest marginal rate bracket for ordinary income, which you may round off to 40%. The amount of individual tax due is not required as part of the answer unless the amount of income tax owed by the individual affects some other aspect of the answer.
(e) Assume that the statutory law and regulations in effect for all years correspond to current law.

7. In writing your answers, observe the following rules:
   (a) Answer questions in complete grammatical sentences.
   (b) Do not use any nonstandard abbreviations.
   (c) Use a section sign — § — for citations to the Code and Regulations.
   (d) Remember that the subsections of the Code and Regulations have parentheses around the letters and numbers. If you omit the parentheses, your citation is incorrect.

8. You may consult only the Code and the Regulations, your case book, any materials distributed by the instructor, your class notes and any other notes that you may have prepared before receiving the examination. All of any outline jointly prepared by a study group in which you have actively and materially participated is treated as materials that you have prepared even though you may not personally have authored particular portions of the outline. No other materials are permitted to be used in answering this examination. You may not use any materials from the law library, commercial study aids, outlines prepared by another student or a study group in which you did not actively and materially participate.

9. This examination answer is to be solely your own work. There is to be no consultation with or receipt of assistance in any form from any other person.

GOOD LUCK and HAPPY HOLIDAYS
1. Amy, Bill, and Chris have come to your law office asking you to represent them in forming a new partnership. They have agreed upon the following terms of the partnership. Amy will contribute $420,000 of cash. Bill will contribute, Sandyacre, which is beachfront property consisting of land and a building. The land has a basis of $20,000 and a fair market value of $60,000. The building has a basis of $520,000 and a fair market value of $360,000. Chris, a building contractor, will contribute services to renovate the building into luxury condominiums that will be sold by the partnership. The venturers expect that most purchasers will use their condominiums only a few weeks a year and will want to rent them out on a weekly basis. They have agreed “to be equal partners.”

(A) Explain to them the significance, particularly with respect to the tax consequences, of the difference between being equal partners in all respects from the outset versus sharing profits and losses equally but taking into account their differing capital contributions in determining rights upon liquidation of the partnership.

(B) Explain to them the tax significance of the difference between the fair market value and basis of Sandyacre.

(C) After the partnership sells the condominiums, the partnership will continue in business as the management agents for the condominium. All three of them will work in that capacity. Bill will take on most of the responsibility of the partnership being the rental manager for those unit owners who will rent their units out on a weekly basis, and will receive 40 percent of the partnership’s gross receipts from this aspect of its management of the condominium complex “off the top,” before the partnership divides its profits between the partners. What are the tax consequences of adding this feature to the agreement?

2. Saints Preservus & Protectus Hospital and Dr. Carter each will contribute $200,000 to form a general partnership. The partnership will purchase a medical office building on leased land for $2,000,000, using the $400,000 contributed by the partners and an additional $1,600,000 borrowed from Leviathan National BanCorp. The promissory note is with full recourse to the partnership. Assume (for simplicity) that the property has a 25 year recovery cost period; the cost recovery method is straight line. Saints Preservus & Protectus Hospital and Dr. Carter intend generally to be equal partners, with the following exceptions:

   (1) Because the Hospital is a tax exempt organization, they want all depreciation deductions to be allocated to Dr. Carter.

   (2) If and when the building is sold and the partnership liquidated, the parties do not want Dr. Carter to have to make an additional contribution to the partnership to fund any possible liquidating distribution to the Hospital, although the parties agree that Dr. Carter could be required to make an additional contribution to repay the mortgage (or any other creditor).

   (3) They don't want the Hospital to receive more than its initial $200,000 cash contribution unless Dr. Carter also receives a liquidating distribution in the
same amount — whatever that amount might be — as is received by the University.

(A) Do the § 704(b) regulations allow a partnership agreement to be written so as to achieve these goals in whole or in part? Explain exactly what the partnership agreement must provide successfully to implement these goals or exactly why these goals cannot be achieved.

(B) Would answer change if the venture were a limited liability company? Why?

3. Jeb and Toni are equal partners of Swampland Realty Development Partnership. Swampland was established quite a few years ago when each member contributed $200,000. Over the years Swampland’s only activity has been the occasional purchase and sale of undeveloped land as speculative investments. The partnership has never actually conducted any development activities. None of the gains have been distributed; all profits have been reinvested by the partnership.

Currently, Swampland has a cash balance in its bank account of $900,000 and owns the following land, subject to the listed mortgages, all of which secure loans incurred to purchase the respective properties:

<table>
<thead>
<tr>
<th>PROPERTY</th>
<th>Basis</th>
<th>F.M.V.</th>
<th>Mortgage</th>
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<tbody>
<tr>
<td>Big Cyprus</td>
<td>$ 500,000</td>
<td>$1,500,000</td>
<td>$400,000</td>
</tr>
<tr>
<td>Paynes Prairie</td>
<td>$1,100,000</td>
<td>$1,000,000</td>
<td>$300,000</td>
</tr>
<tr>
<td>Everglades</td>
<td>$ 300,000</td>
<td>$1,100,000</td>
<td>$200,000</td>
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</tbody>
</table>

Jeb is in need of cash because he is considering changing careers in a few years and needs financing to seek a new position. Accordingly, he wants to dispose of part of his interest in Swampland. Jeb and Toni want your advice about the consequences of structuring the transaction using one of the following three alternatives:

(1) Toni will buy one-half of Jeb's interest in Swampland for $900,000 cash;
(2) Swampland will distribute $900,000 cash to Jeb and his interest will be reduced from a one-half interest to a one-third interest; or
(3) Swampland will distribute Everglades to Jeb and his interest will be reduced from a one-half interest to a one-third interest. Immediately after the distribution Jeb will sell Everglades for $900,000 cash.

What will be the tax consequences of the alternative transactions?