

C. Recommendations Relating to Partnership Tax Issues

1. Strengthen disclosure of disguised sales¹⁵

The Joint Committee staff recommends that the period for which disclosure is required under the disguised sale regulations should be extended beyond two years, and a more detailed disclosure of the source of permanent book-tax differences should be required. For example, extending the disclosure requirement to seven years, the period applicable to contributions and distributions under the pre-contribution gain rules, could make a facts and circumstances determination by the IRS both more likely to occur and easier for the IRS to administer.

2. Strengthen partnership allocation rules¹⁶

Partnership allocations between members of the same affiliated group (and, in general, related parties) may not have the same economic consequences as allocations between unrelated partners. As a result, related partners can use the partnership allocation rules inappropriately to shift basis among assets. The Joint Committee staff recommends strengthening of the anti-abuse rules relating to partnership allocations for property contributed to a partnership, especially in the case of partners that are members of the same consolidated group, to ensure that the allocation rules are not used to generate unwarranted tax benefits.

3. Provide guidance regarding transfers of partial partnership interests¹⁷

The transfer of partial partnership interests among related partners can result in inappropriate basis shifts among the partners. The Joint Committee staff believes that guidance is needed regarding the apportionment of tax basis upon the transfer of a partial partnership interest (particularly when the transfer involves related parties).

4. Provide rules for the appropriate interaction between partnership rules and corporate stock nonrecognition rules¹⁸

The interaction of the partnership basis adjustment rules and the rules protecting a corporation from recognizing gain on its stock can give rise to unintended tax results. Transactions based on this interaction generally purport to increase the tax basis of depreciable assets and to decrease, by a corresponding amount, the tax basis of the stock of a partner.

¹⁵ Further discussion of this recommendation is provided in the description of the transaction known as Project Tomas in Part Three of this Report.

¹⁶ Further discussion of this recommendation is provided in the description of the transaction known as Project Condor in Part Three of this Report.

¹⁷ Further discussion of this recommendation is provided in the description of the transaction known as Projects Tammy I and Tammy II in Part Three of this Report.

¹⁸ Further discussion of this recommendation is provided in the description of the transaction known as Project Condor in Part Three of this Report.

Because the tax rules protect a corporation from gain on the sale of its stock (including through a partnership), the transactions enable taxpayers to duplicate tax deductions at no economic cost. The Joint Committee staff recommends that either (1) the rules protecting a corporation from recognizing gain on its stock should be modified to limit the nonrecognition of any gain if the gain is attributable to a decrease in the tax basis of the stock resulting from the partnership basis adjustment rules, or (2) that the partnership basis adjustment rules should be altered to preclude an increase in the basis of an asset to the extent the offsetting basis reduction would be to stock of a partner (or related party).

In addition, the Joint Committee staff believes that the proposed regulations under section 337, relating to partnership acquisitions of stock of a corporate partner, would preclude taxpayers from engaging in these types of transactions. The Joint Committee staff recommends that final regulations on this subject should be issued expeditiously.