



# NEW YORK STATE BAR ASSOCIATION

One Elk Street, Albany, New York 12207 • PH 518.463.3200 • www.nysba.org

## TAX SECTION

### 2012-2013 Executive Committee

#### ANDREW W. NEEDHAM

Chair  
Cravath, Swaine & Moore LLP  
825 Eighth Avenue  
New York, NY 10019  
212/474-1440

#### DIANA L. WOLLMAN

First Vice-Chair  
212/558-4055

#### DAVID H. SCHNABEL

Second Vice-Chair  
212/909-6336

#### DAVID R. SICULAR

Secretary  
212/373-3082

#### COMMITTEE CHAIRS:

##### Bankruptcy and Operating Losses

Stuart J. Goldring  
Deborah L. Paul

##### Compliance, Practice & Procedure

Elliot Pisem  
Bryan C. Skarlatos

##### Consolidated Returns

Lawrence M. Garrett  
Edward E. Gonzalez

##### Corporations

Karen Gilbreath Sowell  
Linda Z. Swartz

##### Cross-Border Capital Markets

S. Douglas Borisky  
Andrew Walker

##### Employee Benefits

Eric Hillers  
Andrew L. Oringer

##### Estates and Trusts

Alan S. Halperin  
Laura M. Twomey

##### Financial Instruments

Michael S. Farber  
William L. McRae

##### "Inbound" U.S. Activities of Foreign

##### Taxpayers

Peter J. Connors  
Yaron Z. Reich

##### Individuals

Robert E. Brown  
Sherry S. Kraus

##### Investment Funds

Marcy G. Geller  
Joel Scharfstein

##### New York City Taxes

Maria T. Jones  
Irwin M. Slomka

##### New York State Taxes

Paul R. Comeau  
Arthur R. Rosen

##### "Outbound" Foreign Activities of

##### U.S. Taxpayers

Andrew H. Braiterman  
David R. Hardy

##### Partnerships

David W. Mayo  
Eric Sloan

##### Pass-Through Entities

James R. Brown  
John T. Lutz

##### Real Property

Robert Cassanos  
Lisa A. Levy

##### Reorganizations

Peter F. G. Schuur  
Gordon Warnke

##### Securitizations and Structured

##### Finance

Jiyeon Lee-Lim  
W. Kirk Wallace

##### Tax Exempt Entities

Elizabeth T. Kessenides  
Richard R. Upton

## MEMBERS-AT-LARGE OF EXECUTIVE COMMITTEE

Lee E. Allison	Stephen B. Land	Amanda H. Nussbaum	Philip Wagman
Janet A. Andolina	Matthew Lay	David M. Schizer	
Steven A. Dean	Robert J. Levinsohn	Stephen E. Shay	
Kathleen L. Ferrell	Vadim Mahmoudov	Ansgar A. Simon	
Joshua M. Holmes	Gary B. Mandel	Andrew P. Solomon	
Charles I. Kingson	Charles M. Morgan	Eric Solomon	

February 29, 2012

The Honorable Emily S. McMahon  
Acting Assistant Secretary (Tax Policy)  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, DC 20220

The Honorable Douglas H. Shulman  
Commissioner  
Internal Revenue Service  
1111 Constitution Avenue, NW  
Washington, DC 20224

The Honorable William J. Wilkins  
Chief Counsel  
Internal Revenue Service  
1111 Constitution Avenue, NW  
Washington, DC 20224

### Re: Report on Proposed Regulations under Section 469

Dear Ms. McMahon, Mr. Wilkins, and Mr. Shulman:

We write to submit comments on the recent proposed regulations under section 469 of the Internal Revenue Code (the "Proposed Regulations"). Published in the Federal Register on November 28, 2011, the Proposed Regulations propose to modify the current definition of "limited partner" under section 469.

By way of background, section 469(a)(1) limits the ability of individuals and certain other taxpayers to deduct losses from passive activities. For this purpose, a "passive activity" is any trade or business activity in which a taxpayer does not "materially participate." Although most individual partners may establish material participation in an activity under one of seven tests, more restrictive limitations apply to limited partners.

The current temporary regulations treat an interest as a limited partnership interest if it is designated as a limited partnership interest in the partnership agreement or if the holder of the interest has limited liability under the laws of the state in which the partnership is organized. The Proposed Regulations propose to redefine a limited partnership interest as any

## FORMER CHAIRS OF SECTION:

John E. Morrissey, Jr.	Richard J. Hiegel	John A. Cory	Robert H. Scarborough	David S. Miller
Peter L. Faber	Dale S. Collinson	Peter C. Canellos	Robert A. Jacobs	Erika W. Nijenhuis
Hon. Renato Beghe	Richard G. Cohen	Michael L. Schler	Samuel J. Dimon	Peter H. Blessing
Alfred D. Youngwood	Donald Schapiro	Carolyn Joy Lee	Andrew N. Berg	Jodi J. Schwartz
Gordon D. Henderson	Herbert L. Camp	Richard L. Reinhold	Lewis R. Steinberg	
David Sachs	William L. Burke	Richard O. Loengard	David P. Hariton	
J. Roger Mentz	Arthur A. Feder	Steven C. Todrys	Kimberly S. Blanchard	
Willard B. Taylor	James M. Peaslee	Harold R. Handler	Patrick C. Gallagher	

Ms. McMahon  
Mr. Wilkins  
Mr. Shulman  
February 29, 2012  
Page 2

interest in an entity treated as a partnership for federal income tax purposes if the holder thereof does not have “rights to manage” the entity at all times during the entity’s taxable year. The primary rationale for the new definition is that a limited partner may now actively participate in the trade or business of a partnership without becoming subject to unlimited liability under the laws of most states.

We commend the government for abandoning limited liability as the touchstone for distinguishing a limited partner from a general partner. According to the legislative history, Congress presumed at the time of enactment of section 469 that a limited partner who actively participated in the business of a partnership could lose limited liability protection under state law. As described in the preamble, the subsequent elimination of these restrictions in most states, coupled with the birth of LLCs and other entities taxable as partnerships, have largely invalidated this presumption.

Our primary recommendation is that the government revisit the fundamental question of whether the absence of “rights to manage” is the appropriate standard for defining a limited partner in the present legal environment. Given the developments in state law described in the preamble, together with the focus of the statute on material participation in the operations of a trade or business without regard to their nature, we question whether final regulations should continue to perpetuate *any* distinction between types of partnership interests on the basis of attributes that no longer infringe upon the ability of a partner to actively participate in the trade or business of a partnership at any level.

As described more fully in the report, we recommend that final regulations either (i) continue the statutory distinction between a limited and general partner under one of two proposed standards, but allow a limited partner to establish material participation on less restrictive terms; or (ii) abandon the distinction altogether.

If the government decides to retain the “rights to manage” standard in final regulations, we recommend that such regulations provide clear and objective guidance regarding its meaning, including specific examples of the types of rights that will or will not qualify. We also provide a number of other technical comments and recommendations.

We appreciate your consideration of our recommendations.

Respectfully submitted,



Andrew W. Needham  
Chair

Enclosure

Ms. McMahon  
Mr. Wilkins  
Mr. Shulman  
February 29, 2012  
Page 3

cc: Jennifer Alexander  
Attorney-Advisor (Tax Policy)  
Department of the Treasury

Michala Irons  
Office of Associate Chief Counsel (Passthroughs and Special Industries)  
Internal Revenue Service

Beverly Katz  
Special Counsel to the Associate Chief Counsel (Passthroughs and Special Industries)  
Internal Revenue Service

Christopher Kelley  
Special Counsel to the Associate Chief Counsel (Passthroughs and Special Industries)  
Internal Revenue Service

Curt Wilson  
Associate Chief Counsel (Passthroughs and Special Industries)  
Internal Revenue Service

Lisa Zarlenga  
Tax Legislative Counsel (Regulatory Affairs)  
Department of the Treasury