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January 23, 2012

The Honorable Emily S. McMahon
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Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

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

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

Re: Proposed Regulations Withdrawing the *De Minimis* Exception from the Section 704(b) Regulations

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

We are pleased to submit New York State Bar Association Tax Section Report No. 1256. This report conveys the recommendations and comments of the tax section of the New York State Bar Association regarding proposed regulations (the "Proposed Regulations") withdrawing

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the *de minimis* exception of Treas. Reg. § 1.704-1(b)(2)(iii)(e) (“the *De Minimis* Exception”) from the regulations under section 704(b), and responds to the request for comments in the preamble to the Proposed Regulations on how to reduce the burden of complying with the substantial economic effect rules, with respect to look-through partners, without diminishing the safeguards that the rules provide.

For the reasons discussed in the report, we agree that the *De Minimis* Exception should be withdrawn. The report further recommends that the final regulations should apply to all allocations made for partnership taxable years ending on or after the effective date of those regulations, regardless of when the provisions requiring those allocations became a part of the relevant partnership agreement. In addition, the report recommends that the Treasury Department (“Treasury”) and the Internal Revenue Service (“IRS”) publish a notice providing that the provisions of the Proposed Regulations, when finalized, will be effective for partnership taxable years ending on or after the date of the notice.

The report observes that, to determine whether a partnership’s allocations are substantial, a partnership must know the tax attributes of its partners. Because partnerships (such as real estate partnerships and other investment partnerships) typically are comprised of partners that are themselves partnerships or other passthrough entities, it often is difficult or impossible for partnerships to obtain the necessary information about their ultimate partners.

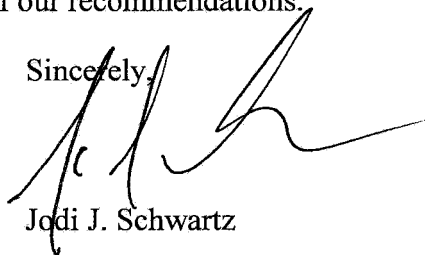
Accordingly, the report recommends that future guidance allow partnerships to make reasonable assumptions about certain classes of partners. Specifically, the report recommends that Treasury and the IRS promulgate regulations that permit partnerships to apply the substantiality tests of Treas. Reg. § 1.704-1(b)(2)(iii) based on reasonable assumptions about (i) the tax attributes of any partner that owns (directly, indirectly, and through attribution) not more than a 5 percent interest in the capital or profits of the partnership (each, a “*De Minimis* Partner”) and (ii) the identity and tax attributes of any person that owns an interest in the partnership indirectly through one or more “look-through entities” within the meaning of Treas. Reg. § 1.704-1(b)(2)(iii)(d)(2) other than disregarded entities (each, an “Indirect Partner”), but only if, in the aggregate, those *De Minimis* Partners and Indirect Partners do not own more a 30 percent interest in the profits and capital of the partnership.

Whether a partnership’s assumptions about the identity and tax attributes of these partners are reasonable should be determined based on all of the facts and circumstances, as illustrated by several examples in the report. The report recommends that future regulations require the partnership to make reasonable inquiries regarding the tax attributes of all of its “*De Minimis* Partners” and the identity and tax attributes of its “Indirect Partners” if the partnership desires to rely on the reasonable assumptions rule. If a partnership relies on this rule, then, provided the partnership’s assumptions are reasonable, allocations that would be substantial on the basis of those reasonable assumptions would be respected even if those assumptions later are determined to have been incorrect.

The Honorable Emily S. McMahon
The Honorable William J. Wilkins
The Honorable Douglas H. Shulman
January 23, 2012
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We appreciate your consideration of our recommendations.

Sincerely,

A handwritten signature in black ink, appearing to read "Jodi J. Schwartz". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Jodi J. Schwartz

Enclosure

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