



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: Deborah A. Butler
Assistant Chief Counsel (Field Service) CC:DOM:FS

SUBJECT: Tax Court Appointment of TMP or Class Representative

This Field Service Advice responds to your memorandum dated September 22, 1999. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND

Mr. A =
Mr. B =
Date 1 =
Date 2 =
Date 3 =
State Law Cites =

X =

ISSUES

1. Whether the substantive consolidation of a group of related partnerships for purposes of a bankruptcy proceeding serves to merge or consolidate the

partnerships such that a partner in a single partnership is deemed to be a partner in all of the partnerships.

2. Whether the Tax Court may appoint a nonpartner to serve as tax matters partner in a case that is pending before it.

CONCLUSIONS

1. The substantive consolidation of a group of related partnerships for purposes of a bankruptcy proceeding does not merge or consolidate the partnerships. A partner in one of the substantively consolidated partnerships is not deemed to be a partner in all of the partnerships.
2. The Tax Court may not appoint a nonpartner to serve as tax matters partner in a case that is pending before it. The Tax Court may, however, appoint a representative for a party who may fulfill a role analogous to the role of the TMP.

FACTS

Mr. A is a general partner in each partnership within a group of related tax shelter partnerships. Mr. A is also designated as the tax matters partner of each of these partnerships. On Date 1, all partnerships were substantively consolidated into a single entity for purposes of an ongoing bankruptcy proceeding. On Date 2, Mr. A was indicted for matters relating to the tax shelter partnerships. In a related partnership item proceeding before the Tax Court, the Service filed a motion pursuant to T.C. Rule 250(b) to remove Mr. A as TMP. In response to the Service's motion to remove the TMP, counsel for Mr. A filed a response indicating that Mr. A would resign as TMP if Mr. B were substituted as TMP. Mr. B is a partner in some, but not all, of the related partnerships.

LAW AND ANALYSIS

The position of the tax matters partner (TMP) is statutorily created and does not exist outside of the TEFRA partnership proceeding context. Specifically, I.R.C. § 6231(a)(7) establishes the position of the TMP, who is imbued with certain rights and responsibilities as set forth throughout the TEFRA partnership provisions. Section 6231(a)(7) also imposes certain limitations on who may be designated to serve as TMP. To be designated by the partnership, the TMP must be a general partner. I.R.C. § 6231(a)(7)(A). Absent a valid designation by the partnership, the general partner with the largest profits interest is the TMP by operation of law.

I.R.C. § 6231(a)(7)(B). If it is impracticable to apply the largest profits interest rule, then the Service may select any partner as TMP, regardless of whether the partner is a general or limited partner.

TMP Designation by the Parties

With regard to designations made by the partnership, the regulations provide that the partner must have been a general partner either at any time during the taxable year at issue or at the time the designation was made. Treas. Reg.

§ 301.6231(a)(7)-1(b). The largest profits interest rule is only applied, however, based upon the partner's interests at the close of the taxable year at issue. Treas. Reg. § 301.6231(a)(7)-1(m)(2). Similarly, a selection by the Service may include any partner who was a partner at any time during the taxable year at issue. Treas. Reg. §§ 301.6231(a)(7)-1(p)(1) and -1(q)(1).

In the instant case, Mr. A has been indicted, and as a result, the Service has sought his removal as TMP. The representative of the current TMP has suggested Mr. B as a replacement; yet for a majority of the partnerships, Mr. B is not a partner. The statute and the regulations promulgated thereunder are clear and unambiguous: a TMP designated by the partnership must be a general partner. To the extent that Mr. B is not a partner in some of the partnerships, he may not be designated to be the TMP for those partnerships.

It has been suggested that the substantive consolidation of the partnerships in the bankruptcy proceeding may, in effect, make Mr. B a current partner in all of the consolidated partnerships. If correct, Mr. B could be designated as TMP because he would be a general partner at the time the designation was made. See Treas. Reg. § 301.6231(a)(7)-1(b)(1)(ii). The Judgment for Substantive Consolidation in the bankruptcy proceeding states as follows:

7. Neither the order granting the motion for summary judgment for substantive consolidation nor this judgment shall be dispositive of the effects of this consolidation on the rights and liabilities of any partner not named as a defendant in this adversary proceeding, which rights and liabilities shall be determined later as necessary.

The Order is clear that the Judgment for Substantive Consolidation alone does not alter the rights of the partners. Thus, though the partnerships have been consolidated for purposes of the bankruptcy proceeding, the Judgment for Substantive Consolidation, on its face, does not alter the legal structure of the partnerships. This conclusion is further strengthened when viewed in light of the state law regarding the merger or consolidation of partnerships in each of the jurisdictions in which the partnerships were formed. Under each provision, a

merger or consolidation of partnerships must be approved by the partners in order for it to be effective. See State Law Cites.

In light of the foregoing, we conclude that the substantive consolidation of the partnerships for purposes of the bankruptcy proceeding did not serve to merge or consolidate the partnerships for any purpose other than the bankruptcy proceeding. Accordingly, Mr. B is not deemed to be a partner of all of the partnerships and thus may not be designated to serve as the TMP of all related partnerships that are docketed before the Tax Court. Similarly, because Mr. B is not a partner in several of the entities, he would not be the TMP under the largest profits interest rule. Lastly, as a nonpartner, Mr. B cannot be selected to serve as TMP by the Service.

Appointment of a TMP by the Court

Once a partnership item proceeding is docketed before the Tax Court, the court "draw[s] upon its inherent powers as a Court to appoint a tax matters partner...." Computer Programs Lambda, Ltd. v. Commissioner, 90 T.C. 1124, 1127 (1990). Under that inherent power, the Tax Court promulgated T.C. Rule 250(b), which provides that "the Court may appoint another partner as the tax matters partner if the partnership fails to designate a successor tax matters partner within such period as the Court may direct." Though this rule expressly sets forth the Tax Court's authority to designate a TMP, the comment states that "Rule 250(b) is declarative of the Court's inherent supervisory authority under existing law...." 90 T.C. at 1379.

In Computer Programs Lambda, the court stated that it can draw upon its inherent powers "in order to protect the rights of partners interested in the partnership proceeding before us and to assure the fair, efficient, and consistent disposition of partnership litigation pursuant to section 6221 et. seq...." Expanding on this point, the court noted that the power to appoint a TMP is analogous to the power of a federal court under Fed. R. Civ. P. 23(d) to issue an "order to fulfill its responsibilities as guardians of the rights of absentee class members and to ensure the orderly progress of the action." Computer Programs Lambda, 90 T.C. at 1127. The power to appoint a lead counsel to represent a class is not expressly set forth in Fed. R. Civ. P. 23(d), yet the Tax Court cited to several cases in which Federal courts have made such appointments. In Cullen v. New York State Civil Service Comm'n, 566 F.2d 846, 849 (2d Cir. 1977), the court explained:

Since absent class members are conclusively bound by the result of an action prosecuted by a party alleged to represent their interests, the court's selection of counsel for the absent class should be guided by the best interests of those members, not the entrepreneurial initiative of the named plaintiffs' counsel. In making a class certification decision, a district court must frequently select as lead counsel for the class the attorney who will best serve the interests of its members. And the court may also find it necessary

to appoint additional counsel to protect the interests of subclasses. See 7 Wright & Miller, Federal Practice and Procedure, Civil § 1765 at 617-623 (1972); 1 Moore's Federal Practice, Part 2, § 1.44 at 50-51 (2d ed. 1977).

The TMP, though serving a vital role, has far less influence on the litigation than the lead counsel in a class action suit. The primary function of the TMP is to keep the nonparticipating partners apprised of the ongoing proceeding. As a mere conduit for information, clearly the court would have the authority to appoint a representative to serve in this capacity even though this person may not technically qualify to serve as TMP.

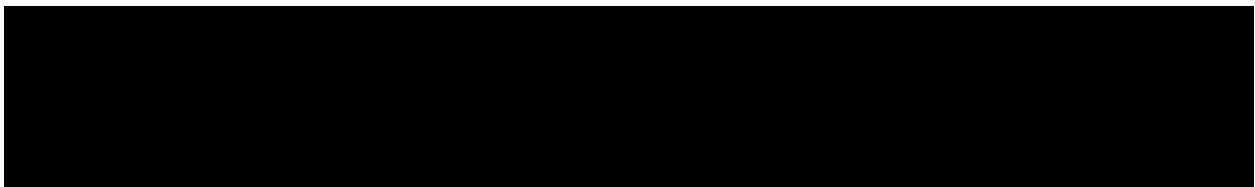
The inherent powers of federal courts are those which "are necessary to the exercise of all others." Roadway Express, Inc. v. Piper, 447 U.S. 752 (1980), quoting United States v. Hudson, 7 Cranch 32, 34 (1812). These powers are those "deemed necessary to protect the efficient and orderly administration of justice and those necessary to command respect for the court's orders, judgments, procedures, and authority." In re Stone, 986 F.2d 898, 902 (5th Cir. 1993). Furthermore, inherent powers include "those reasonably useful to achieve justice."

This category of powers recognizes that the legislature cannot foresee every tool the courts might need to employ to reach a result in all cases. Where it appears that a court cannot adequately and efficiently carry out its duties without employing some special device, the court has inherent power to do so.

Id.

In the instant case, there are over X docketed cases in which the TMP will ultimately need to be removed. A motion is presently pending in several of those cases, and to protect the orderly and efficient administration of justice, it would be appropriate for the court to appoint a single representative for all of these cases. That representative may not qualify under section 6231(a)(7) to serve as TMP; however, under the court's inherent powers, it may appoint a representative outside of this provision. Pursuant to the court's inherent powers, Mr. B may be appointed as a representative in these related TEFRA partnership cases.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS





If you have any further questions, please call the branch telephone number.

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