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TITLE: Identifying Partners' Interests in Partnership Profits and Capital

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PANEL: Identifying Partners' Interests in Partnership Profits and Capital

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COMMITTEE: Partnerships & LLCs

Identifying Partners' Interests in Partnership Profits and Capital

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Relevance

- Measurement of partner's interest in Capital and/or Profit relevant to over 250 Code and regulation provisions
- Examples:
  - §267(b)(10) (denial of losses; referenced in other sections)
  - §351(g) (dirty preferred - related party)
  - §706(b) (taxable year of partnership)
  - §707(b) (transactions with related partners/partnerships; referenced in other sections)
  - §708(b) (terminations, mergers, divisions)
  - §861 (sourcing – related party)
  - §6038 (foreign partnership information reporting)

Policy goals

- Avoid inappropriate tax games with related parties.
- Limit scope of certain tax benefits to unrelated parties (e.g., §29/45K tax credit requires sales to unrelated parties).
- What level of relatedness is appropriate for the goal of the particular provision?

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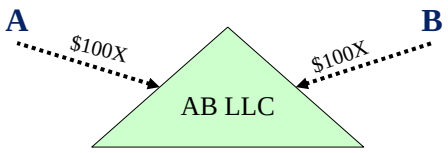
Example 1: 50:50 Base Case



- Facts:
  - A and B each contribute $100x to an LLC and share profits, losses, and risk of loss equally
  - No mandatory capital calls
  - Follows §704(b) safe harbors
- What is interest in capital or profits?
- What if AB LLC has net loss for year?

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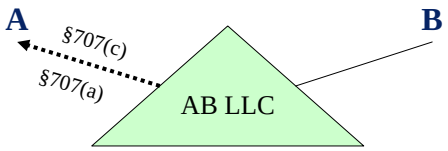
Example 2: §707 Payments



- Facts –50:50 Base Case except:
  - $50x §707(c) payment to A for services; OR
  - 5% §707(a) allocation to A of gross revenue for services.
- What is A's interest in profits?
- Should there be a difference between §707(a) and §707(c)?

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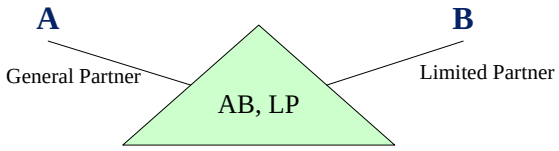
Example 3: Limited Partnerships



- Facts - 50:50 Base Case except:
  - GP/LP split. A is a general partner with full risk of loss (no indemnification). B is a limited partner with no risk of loss beyond capital account.
  - Losses over $200X allocable solely to A.
  - Net income allocated to A, to charge back prior specially allocated losses, and then 50:50.
- Does A have greater than 50% of profits? When?
- Does A have less than 50% of capital after first $200X of losses?

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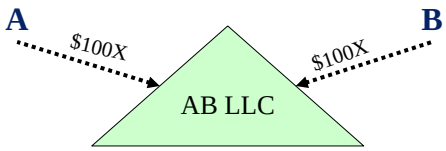
Example 4: Varying Distributions



- Facts – 50:50 Base Case except :
  - Net income allocated to charge back loss allocations and then 75% to A and 25% to B
  - Net losses allocated to charge back profit allocations and then 50% to A and 50% to B
  - Distributions: (1) return capital;
    (2) 75% to A and 25% to B

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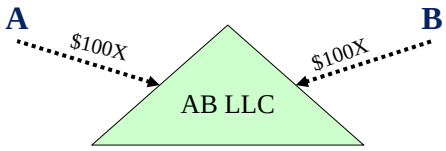
Example 5: Special Allocations of Nonrecourse Deductions



- A and B each contribute $100x to an LLC, no capital calls, follows §704(b) safe harbors
- AB LLC buys Building with nonrecourse debt
- General profit and loss allocations 50:50
- Special allocations of Building depreciation 75% to A and 25% to B, subject to gain chargeback

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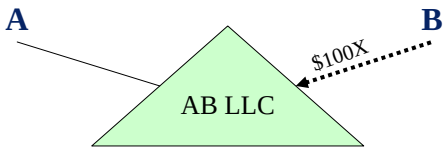
Example 6: Profits Only Interest



- Facts - Base Case except :
  - B is the only partner contributing $100X
  - A received Rev. Proc. 93-27 “profits interest”
  - Net income allocated to chargeback loss allocations and then 50% to A and 50% to B
  - Net losses allocated to chargeback profit allocations and then 100% to B
  - Distributions: (1) return contributed capital;
    (2) 50% to A and 50% to B

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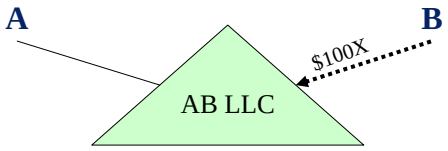
Example 7: Targeted Allocations



- A is a profits only partner, same as Example 5
- Target Distributions:
  - Return of capital
  - 8% preferred return to B
  - 50:50 to A and B
- Profit and Loss allocated to bring capital accounts to equal Target Distribution amounts

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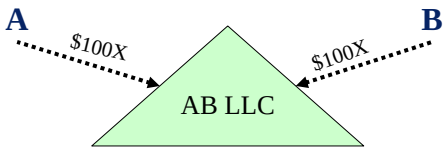
Example 8: Profits Vary by Income Source



- A and B each contribute $100x to LLC
- Operating income and loss:
  - 50% to A
  - 50% to B
- Capital Event income and loss:
  - 25% to A
  - 75% to B

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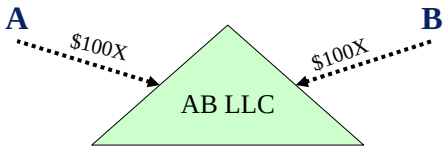
Example 9: Disproportionate Capital and Profits Interests



- A and B each contribute $100x to an LLC
- Profits, losses, and distributions
  - A: 60%
  - B: 40%

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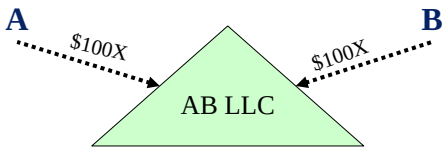
Example 10: Priority Allocation



- A and B each contribute $100x to an LLC
- A receives preferred return of capital and 5% preferred return on capital
- All other allocations 50:50
  - Alternative #1: A's preferred return based on net profits
  - Alternative #2: A's preferred return based on gross income

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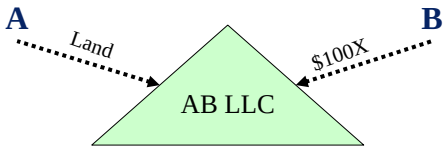
Example 11: § 704(c) Built-In Gain



- Facts –50:50 Base Case except:
  - A contributes land with $50x basis and $100x FMV
  - B contributes $100x in cash to an LLC
- Land sold for $200x
  - $50x §704(c) gain allocated to A;
  - $100x additional gain allocated 50:50

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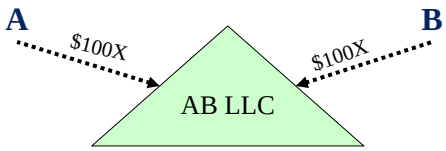
Example 12: Deferred Allocations



- A and B each contribute $100x to an LLC, no capital calls, follows §704(b) safe harbors
- Year 1: 100% profit and loss to A
- Year 2: 100% profit and loss to B
- After Year 2:
  - 50% to A
  - 50% to B

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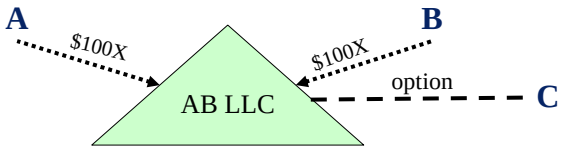
Example 13: Noncompensatory Options



- A and B each contribute $100x to an LLC, no capital calls, follows §704(b) safe harbors – including proposed "corrective allocation rules"
- C receives noncompensatory option
  - $100x Strike Price
  - Entitled to one-third interest on income/losses/distributions
- C exercises option
  - LLC's assets appreciated from $200x to $600x

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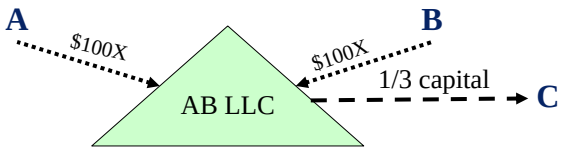
Example 14: Compensatory Capital Interest



- A and B each contribute $100x to an LLC, no capital calls, follows §704(b) safe harbors
- C receives compensatory capital interest
  - Entitled to one-third interest in income/losses/distributions
  - No "liquidation value election"
  - At issuance, FMV of C's interest is $50x (liquidation value is $66.67x)
  - C's initial capital account is $50x but is entitled to $66.67x if AB LLC liquidated

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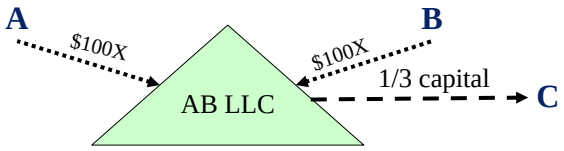
Example 15: Substantially Unvested Compensatory Interest



- Same as Example 14 except that C's interest is subject to 5-year "cliff" vesting
- C forfeits interest in year 4
- "Forfeiture allocations" of $30x deductions to C and remaining allocations 50:50

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Planning/Traps

- Strategic planning to obtain or avoid "relatedness":
  - Guaranteed Payments
  - Preferred Returns
  - Fees
  - Debt versus Equity
  - Other
- In the absence of guidance, are tax practitioners required to follow the "lowest common denominator" approach?

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Policy

- Uniformity versus variability:
  - Should there be uniform definitions of partners' interests in capital or profits or section-by-section definitions?
  - Should "relatedness" percentage be uniform or section-by-section? And, if the latter, what are the appropriate considerations?
  - If uniformity is appropriate, who should decide and implement?

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Policy

- Corporate Analogies
  - Why is vote/value important to corporations and profits/capital important to partnerships?
  - What about entities that switch from one regime to the other?
- Alternatives?
  - Voting power in partnerships (over what?)
  - FMV
  - Others?

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Conclusions

- Current capital and profits interest measurement is a morass.
- As pervasive as “relatedness” is in the tax area, administrability and predictability indicate that the area should receive attention and guidance.

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ABA Section of Taxation
Partnerships and LLCs Committee
Denver, Colorado
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"Identifying Partners' Interests in Partnership Profits and Capital"

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I. ***Introduction***

A. The Problem

1. A large and increasing number of Code provisions, regulations and rulings (both inside and outside Subchapter K) refer to the ownership percentages of a partner's interest in partnership profits ("PIPP") and/or a partner's interest in partnership capital ("PIPC"). The operative consequences of meeting (or failing to meet) the requisite percentage interest in profits and/or capital can have profound favorable or unfavorable tax consequences, affecting all types of partners and partnerships.

2. As discussed below, guidance is lacking as to the definition and measurement of PIPP and PIPC.

B. Relevance to Practitioners and Clients

Measurement of PIPP and/or PIPC are relevant in over 250 provisions of the Code and regulations. Among the more relevant to taxpayers and practitioners are:

1. Section 267(b)(10): denial of losses.

2. Section 351(g): 'dirty' preferred-related party.

3. Section 708(b)(1)(B): consequences arising from operation of the partnership termination rules.

4. Section 707(b): disallowance of losses from sales or exchanges of property involving partnerships and/or partners.

5. Section 706(b): determination of the partnership's taxable year.

6. Section 861: apportionment of interest expense.

7. Form 1065, Section M-3 reporting: consolidation of partnerships' reporting data.

8. Throughout the Code: Any time Sections 267(b) and 707(b) are operative; derivative effects on corporations, individuals, partnerships with foreign-source income, partnerships with tax-exempt partners, foreign partners, etc.

C. "Relatedness"

Presumably, the general goal of the delineations which use PIPP and/or PIPC is to distinguish between the ownership of economic interests in the pass-through entity that meet or fail to meet some policy of "relatedness" underlying the applicable Code provision. Stated simply, when a partner has a specified ownership interest in a partnership, certain tax consequences may arise. When a partner does not have the specified ownership interest, different tax consequences may arise. The specified ownership interest is typically measured with respect to PIPP and/or PIPC.

D. Measuring "Relatedness" via PIPP and PIPC

1. The level of ownership which establishes "relatedness" varies from provision to provision. In some cases, a threshold as high as 80% of PIPP or 90% of PIPC must be reached for the relevant Code provision to cause relatedness to occur. At the other extreme, some Sections provide that any ownership interest in the partnership technically causes sufficient "relatedness" to trigger operative tax consequences. Several hundred other Code and regulations provisions delineate "relatedness" based upon any of a number of percentages that fall somewhere in between.

2. In some cases, only PIPP is the relevant measurement stick; in others, only PIPC is relevant. In many cases, the presence of a sufficient percentage interest in either PIPP or PIPC triggers the operative Code provision. In a few cases, the requisite percentage of both PIPP and PIPC must be met to cause the operative provision to apply.

E. Partnership Percentage Interest Thresholds

1. See Appendix

2. Observations

F. Definitional Uncertainties

There is a lack of uniformity as to the definitions of the terms "partnership profits interest" and "partnership capital interest." In addition, there is a lack of guidance as to how PIPP and PIPC are measured. What little guidance exists is not always consistent. In a tax system where numerous significant operative tax consequences (favorable or unfavorable) may arise, this potentially raises serious problems of administration and compliance with the relevant tax rules.

G. 'Straight Up' Partnerships vs. 'Slice and Dice' Partnerships

1. Under the 1954 Code

2. Today's Sophisticated World

II. ***Survey of Operative Code Provisions***

A. Identifying Operative Code and Regulations Provisions Involving PIPP and/or PIPC

B. The Importance of Measuring PIPP and PIPC Both Inside and Outside of Subchapter K

III. ***Identifying Definitional and Measurement Issues Arising in PIPP***

A. What is a "Profits Interest"?

B. Discussion Models

1. Purpose: to identify a variety of methods (each having some merit) which can be utilized in measuring PIPP

2. In defining PIPP, should we include or exclude items such as guaranteed payments, built-in gains under Section 704(c), mandatory minimum gain and partner minimum gain chargebacks, qualified income offsets, curative allocations of income and gain, and other 'mechanical' gain or income allocations mandated by the complex Regulations under Section 704?

3. If so, which, when, how, and to what extent?

4. In defining PIPP, should anything turn on the partner's interest in partnership losses? Is "relatedness" only relevant based on one's share of partnership profits?

C. The ALI Project

IV. ***Definitional and Measurement Issues in PIPC***

A. What is a "Capital Interest"?

1. Tax, book, Section 704(b) and other definitions

2. Does PIPC change daily?

3. Does a partner's interest in his or her allocable share of partnership losses affect PIPC?

B. Discussion Models

C. The ALI Project

V. ***Practical and Administrative Aspects of Identifying PIPP and PIPC***

A. Retroactive Allocations

B. Measuring PIPP and PIPC Where the Partnership Owns Multiple Properties with Differing Allocations

C. Operative Tax Consequences of Changes or Shifts in Profits Interest

D. Inconsistent Reporting Positions by the Partnership and its Partners as to the Measurement of PIPP and PIPC

VI. ***Planning Opportunities (and Traps For the Unwary) Arising Under the Meanings of PIPP and PIPC***

A. Strategic Planning

B. Using Guaranteed Payments or Preferred Returns

C. Fees to Affiliates

D. Debt in Lieu of Additional Equity

E. Limited Partnerships: Special Problems

F. Determining PIPP in Loss Years

G. Others Too Good to Put in Print

VII. ***Conceptual Issues***

A. Should there be uniform definitions of PIPP and PIPC, respectively, for all purposes of the Code, or should they evolve on an operative Code Section–by–Code Section basis?

B. Why is the line of percentage demarcation drawn in various operative Code Sections and Treasury Regulations where it is? Should the percentage be made uniform?

C. If a uniform definition is appropriate, is it within the domain of Congress, Treasury or IRS to provide?

D. What's Happening in the Field: Tales from the Front

1. How does the system (read: IRS) currently deal with these definitional and measurement problems?

2. Congress to Treasury to IRS to Congress: When in doubt, punt!

3. How are the courts likely to respond?

4. The LCD Approach: In the absence of guidance, are tax practitioners required to follow the "lowest common denominator" (LCD) approach, i.e., certainty exists only if all possible interpretations of what constitutes the measurement of partnership profits or capital are met (or failed)?

VIII. ***The Corporate Analogue***

A. What are the Corporate Measurement Sticks for "Relatedness"?

Do the concepts of "relatedness" contained in the Code and regulations with respect to corporate stock ownership provide any useful guidance or benchmarks in thinking about "relatedness" among partners?

B. Thinking About the Differences

Are the methodologies or the measuring sticks used in determining corporate "relatedness" (in comparison to those used for PIPP and PIPC) different but good, different but bad, or just plain "different"?

C. Corporations are from Venus, Partnerships are from Mars

1. Picture a multi-member LLC which is initially taxed as a partnership

2. In a later year the LLC elects to be taxable as a corporation (with no change in ownership, economic rights, liabilities or obligations)

3. Compare the different regimes that apply to the same owners of the same state law unincorporated entity in determining whether "relatedness" exists

IX. ***Alternative Approaches to "Relatedness" for Partnerships and Partners***

A. If PIPP and PIPC were not the measuring rods for most "relatedness" purposes, what alternative or supplemental approaches can be provided which are viable and administrable?

B. Is the presence or absence of voting power relevant for determining relatedness?

C. Should the fair market value of each partner's interest be the sole arbiter of whether relatedness exists in the partner/partnership context? Should Section 704(b) values be used to measure fair market value?

D. Are there other approaches?

E. What are the advantages and disadvantages of each alternative?

F. Should there be a uniform alternative approach, which takes the place of PIPP and PIPC throughout the Code, regulations and other governmental guidance?

1. If so, is it solely within the domain of Congress to implement such a change?

2. Can Treasury unilaterally amend its regulations on PIPP and PIPC to initiate an alternative approach, if the Code does not explicitly mandate PIPP or PIPC?

X. ***Observations and Conclusions***

APPENDIX I

PARTNERSHIP INTERESTS IN CAPITAL AND/OR PROFITS

The following is a catalog of Code and regulatory provisions which may have significant tax consequences, depending upon the measurement of PIPP and PIPC:

1. For purposes of allocating the new markets tax credit under Section 45D, an "equity investment" includes **any capital interest** in a partnership. (Section 45D(b)(6)(B).) The Secretary is directed to give priority to any entity that (among other things) intends to make "qualified low-income housing investments" in one or more businesses in which persons unrelated to such entity hold the **majority equity interest.** (Section 45D(f)(2)(B).)

2. For purposes of investment credit allocation under Section 46 (since amended), each partner will take into account separately his share of the basis of partnership new Section 38 property and his share of the cost of partnership used Section 38 property placed in service by the partnership during such partnership taxable year. Each partner's share of the basis (or cost) of any Section 38 property was determined in accordance with the ratio in which the partners **divide the general profits of the partnership**. (Reg. Section 1.46-3(f)(2).)

3. For purposes of determining a "parent-subsidiary group under common control" (being thereby a group of "trades or businesses that are under common control" as used in Section 52), a chain of organizations that are deemed connected through ownership of a "controlling interest" includes, in the case of a partnership, ownership of **more than 50% of the profit interest or capital interest** in the partnership. (Reg. 1.52-1(c)(2)(iii).) Similarly, in determining a "brother-sister group under common control," a "controlling interest" includes, in the case of a partnership, ownership of **at least 80% of the profit interest or capital interest** of the partnership. (Reg. 1.52-1(d)(2)(iii).) For purposes of determining whether "effective control" exists, the term means, in the case of a partnership, ownership of **more than 50% of the profit interest or capital interest** of the partnership. (Reg. 1.52-1(c)(3)(iii).)

4. In determining the amount taxable as a fringe benefit, special rules relate to a "control employee," which is any employee who owns a **1% or greater equity, capital or profits interest** in the employer. (Reg. 1.61-21(f)(5)(iv).) For certain valuation rules relating to non-commercial flight valuation, a "control employee" includes any employee who owns a **5% or greater equity, capital or profits interest** in the employer. (Reg. 1.61-21(g)(8)(i)(C).)

5. Discharge of indebtedness income is created when a taxpayer's debt is acquired at a discount by a related person, defined as including a person related under Section **707(b)(1)**. (Section 108(e)(4)(B); Reg. 1.108-2(a), (d)(2)(i).)

6. Deductions for amounts contributed under qualified group legal services plans are disallowed if excess payments are made on behalf of a partner who owns **more than 5% of the capital or profits interest** in the employer. (Section 120(c)(3); Prop. Reg. 1.120-2(f)(2)(ii).)

7. Exclusions from gross income from educational assistance programs for principal owners (or their spouses or dependents), each of whom (on any day of the year) owns **more than 5% of the capital or profits interest** in the employer. (Section 127(b)(3); Reg. 1.127-2(f)(ii).)

8. For purposes of the interest stripping rules of Section 163(j), a special rule as to "related persons" applies for certain partnerships. Any interest paid or accrued to a partnership which would be a related person (but for this exception) will not be treated as paid or accrued to a related person if **less than 10% of the profits and capital interests** in such partnership are held by persons with respect to whom no federal income taxes are imposed on such interest. (Section 163(j)(4)(B)(i).)

9. The interest stripping rules of Section 163(j) may disallow the interest deduction in certain circumstances for interest where there is a disqualified guarantee of such indebtedness. Such does not include a guarantee if, e.g., the taxpayer owns a controlling interest in a guarantor partnership; a "controlling interest" being defined as **at least 80% of the profits and capital interests** of the partnership. (Section 163(j)(6)(D)(ii).)

10. For purposes of Section 267(b), a related person includes a corporation and a partnership if the same persons own (i) more than 50% in value of the outstanding stock of the corporation and (ii) **more than 50% of the capital or profits interest** in the partnership. (Section 267(b)(10).)

11. With respect to Section 267(a)(1) applying if the other requirements of Section 267(a)(1) are met: if the two partnerships have one or more common partners (i.e., if any person owns directly, indirectly or constructively **any capital or profits interest** in each of such partnerships), a portion of the selling partnership's loss will be disallowed under Section 267(a)(1) (subject to a de minimis test). (Reg. Section 1.267(a)-2T(c), Answer 2.)

12. If the other requirements of Section 267(a)(2) are met, Section 267(a)(2) applies to defer an otherwise deductible amount arising as a result of transactions entered into between two partnerships which have one or more common partners (i.e., if any person owns directly, indirectly, or constructively **any capital or profits interest** in each of such partnerships). (Section 267(e)(1)(C).)

13. For purposes of Section 267(a)(2), in the case of a partnership, any person who owns (directly or indirectly) **any capital interest or profits interest** of such partnership shall be treated as persons specified in Section 267(b). (Section 267(e)(1)(B)(i).)

14. For purposes of Section 267(b), there is an exception to the disallowance rule with respect to qualified expenses and interest paid or incurred by a partnership owning low-income housing to any qualified 5% or less partner of such partnership. A "qualified 5% or less partner" means any partner who has **an interest of 5% or less in the aggregate capital and profits interests** of the partnership and who meets certain other requirements. (Section 267(e)(5)(A)(i) and (B).)

15. For purposes of determining the value of a transferee foreign corporation under Reg. 1.367(a)-3(c)(3)(iii)(A), assets acquired outside the ordinary course of business by the transferee within the 36-month period preceding the exchange may include certain interests in a

qualified partnership. (Reg. 1.367(a)-3(c)(3)(iii)(B)(1)(ii).) A "qualified partnership" in general is a partnership in which the transferee foreign corporation, inter alia, owns a **25% or greater interest in the partnership's capital and profits**. (Reg. 1.367(a)-3(c)(5)(viii)(A)(2).) However, a partnership is not a "qualified partnership" if the U.S. target company or any of its affiliates held **a 5% or greater interest in the partnership's capital and profits** at any time during the 36-month period prior to the transfer. (Reg. 1.367(a)-3(c)(5)(viii)(B).)

16. For purposes of qualified plan treatment with respect to owner-employees, in the case of a partnership, it is a partner who owns **more than 10% of either the capital interest or the profits interest** in such partnership. (Section 401(c)(3)(B); Reg. 1.401-10(d).)

17. For purposes of identifying qualified plans covering an owner-employee, or group of owner-employees, who control another trade or business, "control" is defined to include ownership by the owner-employee(s) of **more than 50% of the capital or profits interest** of a partnership. (Reg. 1.401-12(l)(3)(i)(*b*).) (Note: only applicable prior to amendment of Section 401(d)(1)(B) in 1996)

18. For purposes of identifying "two or more trades or businesses under common control" for purposes of Section 414(c), a "controlling interest" exists in the case of a partnership, where there is a parent organization that owns **at least 80% of the profits or capital interest** in such partnership. (Reg. 1.414(c)-2(b)(2)(i)(C).) Similarly, in determining whether the same five or fewer persons are in "effective control" of two or more organizations so as to establish a "brother-sister group of trades or businesses under common control," the threshold is whether such persons own an aggregate of **more than 50% of the profits interest or capital interest** of such partnership. (Reg. 1.414(c)-2(c)(2)(iii).)

19. For purposes of Sections 401, 408(k), 408(p), 410, 411, 415 and 416, all employees of trades or businesses (whether or not incorporated) which are under "common control" are treated as employed by a single employer. (Section 414(c).) If a "parent organization" owns, in the case of a partnership, **50% or more of the profits or capital interest** of such partnership, then for purposes of determining whether the parent organization or such other (subsidiary) organization is a member of a parent-subsidiary group of trades or businesses under common control, an interest in such subsidiary organization otherwise excluded under Reg. 1.414(c)-3(b)(3), (4), (5) or (6) shall be treated as not outstanding. (Reg. 1.414(c)-3(b)(iii).) Similarly, in determining whether a "brother-sister group of trades or businesses under common control" exists, if "common owners" (as defined in Reg. 1.414-3(c)) own, in the case of a partnership, **50% or more of the profits or capital interest** in such partnership, then for purposes of determining whether such organization is a member of a brother-sister group of trades or businesses under common control, an interest in such organization excluded under Reg. 1.414(c)-3(c)(2), (3) or (4) shall be treated as not outstanding. (Reg. 1.414(c)-3(c)(iii).)

20. For the same purposes, in determining whether an interest which is an interest in or stock of such organization shall be excluded if owned by an organization which is controlled by an individual, estate or trust that is a "principal owner" of such organization, a "principal owner" includes a person who owns, in the case of a partnership, **5% or more of the profits or capital interest** of such partnership. (Reg. 1.414(c)-3(d)(2)(iii).)

21. In determining an "interest in an organization" for purposes of Reg. 1.414(c)-2 and 1.414(c)-3, an interest owned by or for a partnership shall be considered as owned by any partner having an interest of **5% of more in either the profits or capital** of the partnership in proportion to such partner's interest in the profits or capital, whichever such proportion is greater. (Reg. 1.414(c)-4(b)(2).)

22. For purposes of determining a "highly compensated active employee" under Section 414(q), an employee who is a "5% owner" is included. If the employer is not a corporation, a "5% owner" is any employee who owns **more than 5% of the capital or profits interest** of the employer. (Reg. 1.414(q)-1T, Q&A-8.)

23. In determining whether a qualified plan is top-heavy under Section 416, if the employer is not a corporation, a "1% owner" is any employee who owns **more than 1% of the capital or profits interest** in the employer (Reg. 1.416-1, T-16) and a "5% owner" is an employee who owns **more than 5% of the capital or profits interest** in the employer (Reg. 1.416-1, T-17).

24. For purposes of qualifying to elect the taxable year of certain partnerships under Section 444, where **more than 50% of the profits and capital interest** of a partnership are owned by another partnership or S corporation, such entity is treated as a "downstream controlled partnership" and is a member of a tiered structure. Therefore, it must have the same taxable year as all other members of the tiered structure in order to qualify for or maintain the Section 444 election. Similarly, if **more than 50% of a partnership's profits and capital** are owned by a downstream controlled partnership, such owned partnership is also considered a downstream controlled partnership. (Temp. Reg. 1.444-2T(e)(2)(ii).)

25. The installment sales rules under Section 453 do not apply to sales of depreciable property to related persons. For this purpose, "related persons" includes a partnership **more than 50% of the capital or profits interests** in which is owned (directly or indirectly) by or for a taxpayer, as described in Section 1239(b). (Section 453(g)(3).)

26. With respect to a partnership's active business, if the taxpayer corporation is a "qualified corporate partner," and other requirements are met, then the taxpayer's proportionate share of the partnership's activities in such business will be treated as activities of the taxpayer. A "qualified corporate partner" is a corporation that, inter alia, has an **interest of 10% or more in the partnership's profits and losses**. (Section 465(c)(7)(D)(ii)(II).)

27. In determining whether certain rules (applicable before January 23, 1997) under Section 475 apply to items held by a dealer in securities, "control" of a partnership means the ownership of **50% or more of the capital or profits interest** in a widely held or publicly traded partnership. (Reg. 1.475(b)-1(e)(1)(ii)(B).)

28. For purposes of determining whether an organization is exempt from tax under Section 501 as a credit counseling organization, it must **not own more than 35% of the profits interest** of any partnership which is in the trade or business of lending money, repairing credit, or providing debt management plan services, payment processing, or similar services. (Section 501(q)(1)(E)(ii), enacted August, 2006.)

29. For purposes of the depletion allowance under Section 613A(c)(7), the depletion allowance shall be computed separately by the partners, and the partnership shall allocate to each partner his proportionate share of the adjusted basis of each partnership oil or property. A partner's proportionate share of the adjusted basis of partnership property shall be determined **in accordance with his interest in partnership capital or income**. (Section 613A(c)(7)(D); Reg. 1.613A-3(e)(2)(ii).)

30. For purposes of Section 613A(d), a related person is one owning a "significant ownership interest," which, with respect to a partnership, means **5 percent or more interest in the partnership's profits or capital**. (Section 613A(d)(3)(B); Reg. 1.613A-7(m)(1)(ii).)

31. For purposes of the family partnership rules under Section 704(e)(1), an individual's status as a partner can depend upon whether he has **an interest in partnership capital**. Furthermore, the tax consequences to the donee partner can then vary, **depending on the extent of his capital interests**. (Section 704(e)(1); Reg. 1.704-1(e); see ALI Project, page 300.)

32. For purposes of determining the taxable year of a partnership which is determined by reference to the taxable year of all of the principal partners of the partnership pursuant to Section 706(b)(1)(B)(iii), a "principal partner" is defined as "a partner having an **interest of 5% or more in partnership profits or capital**." (Section 706(b)(3).)

33. In determining the taxable year of a partnership, a partnership shall not have a taxable year other than the majority interest taxable year (as defined in Section 706(a)(4)), if there is such a taxable year. A "majority interest taxable year" means the taxable year (if any) which, on each testing day, constitutes the taxable year of one or more partners having (on such day) **an aggregate interest in partnership profits and capital of more than 50%**." (Section 706(b)(4)(A)(i).)

34. For purposes of determining the taxable year of a partnership under Section 706(b), any interest held by a disregarded foreign partner is not taken into account. However, if each partner that is not a disregarded foreign partner under Reg. 1.706-1(b)(6)(i) holds **less than a 10% interest in the capital and profits** of the partnership, and the regarded partners, in the aggregate, hold **less than a 20% interest in the capital and profits** of the partnership, then Reg. 1.706-1(b)(6)(i) shall not apply. (Reg. 1.706-1(b)(6)(iii).)

35. Disallowance of losses from sales or exchanges of property between a partnership and a person owning, directly or indirectly, **more than 50% of the capital interest, or the profits interest,** in such partnership. (Section 707(b)(1)(A); Reg. 1.707-1(b)(1)(i) and (3).)

36. Disallowance of losses from sales or exchanges of property between two partnerships in which the same persons own, directly or indirectly, **more than 50% of the capital interests or profits interests**. (Section 707(b)(1)(B); Reg. 1.707-1(b)(1)(i) and (3).)

37. Whether a partnership has terminated for tax purposes because there has been a sale or exchange of **at least 50% of the interests in partnership profits and capital**. (Section 708(b)(1)(B); Reg. 1.708-1(b)(2).)

38. In determining a distributee partner's net precontribution gain for purposes of Section 737, such is the net gain (if any) that would have been recognized by the distributee partner under Section 704(c)(1)(B) if all property that had been contributed to the partnership immediately before the distribution had been distributed by the partnership to another partner other than a partner who owns **more than 50% of the capital or profits interest** in the partnership. (Reg. 1.737-1(c)(1).)

39. For purposes of determining the amount of a basis adjustment of partnership property in the case of a transfer of an interest in a partnership under Section 743(b), a partner's proportionate share of the adjusted basis of partnership property shall be determined **in accordance with his interest in partnership capital**. (Section 743(b)(2).)

40. For purposes of determining a partner's share of the nonrecourse liabilities of a partnership, **the partner's share of partnership profits** must be determined. For purposes of Reg. 1.752-3(a)(3), PIPP "is determined by taking into account all facts and circumstances relating to the economic arrangement of the partners. The partnership agreement may specify the partners' interests in partnership profits for purposes of allocating excess nonrecourse liabilities provided the interests so specified are reasonably consistent with allocations (that have substantial economic effect under the Section 704(b) regulations) of some other significant item of partnership income or gain...." (Reg. 1.752-3(a)(3).)

41. For purposes of an election out of Subchapter K, an unincorporated organization which has not made the proper form of election shall nevertheless be deemed to have made the election if it can be shown from all the surrounding facts and circumstances that it was the intention of the members of such organization at the time of its formation to secure exclusion from all of Subchapter K beginning with the first taxable year of the organization. Among the facts which may indicate the requisite intent is "the members of the organization owning **substantially all of the capital interest** report their respective shares of the items of income, deductions, and credits of the organization on their respective returns in a manner consistent with the exclusion of the organization from Subchapter K beginning with the first taxable year of the organization." (Reg. Section 1.761-2(b)(2)(ii)(*b*).)

42. For purposes of meeting the 100 partner requirement to be an electing large partnership (ELP) under Section 775, individuals who perform or performed substantial services in connection with the ELP's activities are excluded. For this purpose, the activities of an ELP include the activities of any other partnership in which the ELP owns **at least an 80% interest in the capital and profits** of the lower tier partnership. (Section 775(b)(3).)

43. For purposes of determining a REIT's share of assets (for purposes of the assets test under Section 856), "the trust will be determined to own its proportionate share of each of the assets of the partnership and will be deemed to be entitled to the income of the partnership attributable to such share. For purposes of Section 856, the interest of a partner in the partnership's assets shall be determined **in accordance with his capital interest** in the partnership." (Reg. Section 1.856-3(g).)

44. For purposes of allocating a partner's distributive share of <u>partnership</u> interest expense, such is allocated to the partner's distributive share of the partnership's gross income, in

the case of a partner with a **less-than-10% partnership interest** (except an individual general partner). (Reg. Section 1.861-9T(e)(4)(i).) A partner's distributive share of partnership interest expense is apportioned based on all the assets of the partner, including his pro rata share of all the assets of the partnership, in the case of a partner with a **10%-or-greater interest** (Reg. Section 1.861-9T(e)(2) and (3).)

45. For purposes of allocating a partner's own interest expense, such is apportioned based on all the partner's assets, including the value of the partner's partnership interest, in the case of a partner with a **less-than-10% partnership interest** (except an individual general partner). (Reg. Section 1.861-9T(e)(4)(ii).)

46. For lessors of certain ships, aircraft or spacecraft who lease such craft to a U.S. person that is not a member of the same controlled group of corporations, the lessor must include gross income with respect to the craft as U.S. source income. Solely for purposes of Reg. 1.861-16, **if at least 80% of the capital or profits interest** in a partnership is owned by a member or members of a controlled group of corporations, then the partnership is considered a member of that controlled group. In addition, if **at least 80% of the capital or profits interest** in a partnership is owned by a corporation, then the partnership and that corporation shall be considered members of a controlled group of corporations. (Reg. 1.861-16(d).)

47. For purposes of determining under Section 864(b)(2)(A) whether certain foreign persons are considered to be engaged in trade or business within the U.S. solely because such person is a member of a partnership that effects transactions in the U.S. in stocks or securities for the partnership's own account, under a special exception applies to a member of a partnership in which, at any time during the last half of its taxable year, **more than 50% of either the capital interest or the profits interest** is owned, directly or indirectly, by five or fewer partners who are individuals and that meet certain other requirements. (Reg. 1.864-2(c)(2)(ii).)

48. For purposes of the foreign tax credit limitation under Section 904, a partner will be considered as owning 10% of the value of a partnership for a particular year if the partner owns **10% of the capital and profits interest** of the partnership. (Reg. 1.904-5(h)(4).) This is relevant under look-through rules involving a partner's ownership of 10% or more of the value of a partnership (i.e., Reg. 1.904-5(h)(1)) and for certain partners' ownership of less than 10% of the value in a partnership (i.e., Reg. 1.904-5(h)(2)(i)).

49. For purposes of the foreign tax credit limitation under Section 904 and Reg. 1.904-5T(i)(1), a partnership (the first partnership) is considered as owning more than 50% of the value of another partnership (the second partnership) if the first partnership owns **more than 50% of the capital and profits interests** in the second partnership. (Reg. 1.904-5(h)(4).)

50. For purposes of determining foreign base company income under Section 954, a look-through rule applies in the case of a sale by a CFC of an interest in a partnership with respect to which such corporation is a 25% owner. A "25% owner" means a CFC which owns directly **25% or more of the capital or profits** in a partnership. (Section 954(c)(4)(B).)

51. For purposes of determining foreign base company income under Section 954, a person is a "related person" with respect to a CFC if (i) such person is a partnership which

controls, or is controlled by, the CFC, or (ii) such person is a partnership which is controlled by the same person or persons which control the CFC. For this purpose, in the case of a partnership, "control" means the ownership of **more than 50% (by value) of the capital or profits interest** in the partnership. (Section 954(d)(3); Reg. 1.954-1(f)(2)(ii).)

52. For purposes of basis reductions following a discharge of indebtedness under Section 1017, a taxpayer must request a partnership's consent to reduce inside basis if, at the time of the discharge, the taxpayer owns **a greater than 50% interest in the capital and profits** of the partnership. (Reg. 1.1017-1(g)(2)(ii)(B).)

53. For purposes of basis reductions following a discharge of indebtedness under Section 1017, a partnership must consent to reduce its partners' shares of inside basis with respect to that indebtedness by partners owning an aggregate of **more than 80% of the capital and profits interests** of the partnership, or five or fewer partners owning an aggregate of **more than 50% of the capital and profits interests** of the partnership. (Reg. 1.1017-1(g)(2)(ii)(C).)

54. The nonrecognition rule provided by Section 1033 as to involuntary conversions is not available to (among others) a partnership in which one or more C corporations own **more than 50% of the capital or profits interest** in such partnership at the time of the involuntary conversion. (Section 1033(i)(2)(B).)

55. For purposes of treating gain from sale of depreciable property between certain related taxpayers as ordinary income rather than capital gain, the term "related persons" includes a person and all entities which are controlled entities with respect to such person. A "controlled entity" includes a partnership **more than 50% of the capital or profits interest** in which is owned by or for such person. (Section 1239(c)(1)(B).)

56. For purposes of computing an S corporation's built-in gain during a recognition period, the S corporation includes gain from its distributive share of partnership items unless (i) the S corporation's partnership interest represents **less than 10% of the partnership's capital and profits** at all times during the taxable year and prior taxable years in the recognition period, and (ii) the fair market value of the S corporation's partnership interest as of the beginning of the recognition period is less than $100,000. (Reg. 1.1374-4(i)(5)(i).)

57. For purposes of constructive ownership under the consolidated return rules, stock owned by or for a partnership shall be considered as owned by any partner having an **interest of 5% or more in either the capital or profits** of the partnership in proportion to his interest in capital or profits, whichever such proportion is the greater. (Section 1563(e)(2); Reg. 1.1563-3(b)(2)(i).)

58. For purposes of meeting the requirements for a qualified domestic trust (QDOT), in determining whether no more than 35% of the fair market value of the QDOT assets consists of foreign real property, if the QDOT owns **more than 20% of the capital interest** of a partnership with 15 or fewer partners, then all assets owned by the partnership are deemed to be owned directly by the QDOT to the extent of the QDOT's pro rata share of the partnership's assets. The QDOT partner's pro rata share is based on the greater of its interest in the capital or profits of the partnership. (Reg. 20.2056A-2(d)(1)(ii)(B).)

59. For purposes of the estate tax deduction under Section 2057 for qualified family-owned businesses, the requisite ownership of a partnership carrying on a trade or business so as to constitute a "qualified family-owned business interest" is (i) at least 50% ownership by the decedent's family; or (ii) at least 70% owned by members of two families, or (iii) at least 90% owned by members of three families; with at least 30% of such entity in (ii) and (iii) having been owned by the decedent and members of the decedent's family. Ownership of the partnership is determined by the owning of **the appropriate percentage of the capital interest** in such partnership. (Section 2057(e)(3)(A)(ii).)[1]

60. For purposes of Section 2701, a "controlled entity" includes a partnership by certain individuals holding **at least 50% of the capital or profits interest** in the partnership. (Reg. 25.2701-2(b)(5)(iii).)

61. For purposes of Section 2701, in the case of a limited partnership, "control" means the holding of **any equity interest** as a general partner. (Reg. 25.2701-2(b)(5)(iii).)

62. For purposes of Section 2701, in determining the indirect holding of interests a person is considered to hold an equity interest held by or for a partnership in the proportion that **the fair market value of the larger of the person's profits interest or capital interest** in the partnership bears to the total fair market value of the corresponding profits interests or capital interests in the partnership, as the case may be. (Reg. 25.2701-6(a)(3).)

63. In connection with taxes on excess business holdings of a private foundation, the permitted holdings of a private foundation in a partnership turn on ownership of **a 20% or 35% profits interest** in the partnership. (Section 4943(c)(2)(A), (2)(B) and (3)(A); Reg. 53.4943-1.)

64. The tax on excess business holdings of supporting organizations may apply to an organization which meets certain requirements and is effectively controlled by (or substantially all of the contributions were made by) the same person or persons. Such a "person" is defined to include an owner of **more than 20% of the profits interest** of the partnership. (Section 4943(f)(4)(B)(iii)(II), enacted August, 2006).

65. For purposes of taxes on self-dealing transactions between a trust and a "disqualified person", the latter includes a person who is the owner of **more than 10% of the profits interest** of a partnership which is a contributor to the trust. (Section 4951(e)(4)(C)(ii).) A "disqualified person" also includes a partnership in which certain specified persons own **more than 35% of the profits interest**. (Section 4951(e)(4)(G).)

66. For purposes of the tax on excess benefit transactions under Section 4958, a "disqualified person" includes a partnership in which certain persons own **more than 35% of the profits interest**. (Section 4958(f)(3)(A)(ii); Reg. 53.4958-3(b)(2)(i)(B).)

67. For purposes of the tax on excess benefit transactions under Section 4958, in identifying an "excess benefit transaction," all economic consideration and benefits exchanged

[1] The Senate Committee Report (which Report was followed by the Conference Committee agreement, see Comm. Repts. on P.L. 105-34, TRA 1997) states that an ownership interest of the requisite percentage interest in partnership profits is also required. The statute does not so provide. No regulations have been issued to date to clarify the inconsistency.

with the applicable tax-exempt organizations and all entities the organization "controls" are taken into account. For this purpose, "control" includes the tax-exempt organization's ownership of **more than 50% of the profits or capital interests** in a partnership. (Reg. 53.4958-4(a)(2)(ii)(B)(*1)(ii)*.)

68. In determining whether a prohibited transaction has occurred with respect to a "disqualified person", the latter includes an owner of **50% or more of the capital interest or the profits interest** of a partnership which is an employer or an employee organization described in Section 4975(e)(2)(C) or (D). (Section 4975(e)(2)(E)(ii).) A "disqualified person" also includes a partnership in which **50% or more of the capital interest or profits interest** of such partnership is owned by certain persons having designated relationships with the plan. (Section 4975(e)(2)(G)(ii).) A "disqualified person" also includes **a 10% or more (in capital or profits)** partner or joint venturer of certain persons having designated relationships with the plan. (Section 4975(e)(2)(I).)

69. In connection with information returns required of certain U.S. persons with respect to controlled foreign partnerships (CFPs) under Section 6038, a "controlling 50% partner" means a U.S. person that controlled the foreign partnership, i.e., is owner of more than a 50% interest in the partnership. (Section 6038(e)(3)(A); Reg. 1.6038-3(a)(1).) A "50% interest in a partnership" is **an interest equal to 50% of the capital interest, 50% of the profits interest, or an interest to which 50% of the deductions or losses of such partnership are allocated**. (Reg. 1.6038-3(b)(2).)

70. In connection with information returns required of certain U.S. persons with respect to CFPs, a "controlling 10% partner" is a U.S. person who owned a 10% or greater interest in the partnership while the partnership was controlled by U.S. persons owning 10% or greater interests. (Reg. 1.6038-3(a)(2).) A "10% interest in a partnership" is **an interest equal to 10% of the capital interest, 10% of the profits interest, or an interest to which 10% of the deductions or losses of such partnership are allocated**. (Reg. 1.6038-3(b)(3).)

71. For purposes of the extension of time for payment of estate taxes where the estate consists largely of interests in closely held businesses, which include an interest as a partner in a partnership carrying on a trade or business if **20% or more of the total capital interest** is included in determining the decedent's gross estate. (Section 6166(b)(1)(B)(i); Reg. 20.6166A-2(a)(2).)

72. With respect to IRS administrative proceedings, IRS does not have to mail notices to each partner if the partnership has more than 100 partners and the partner has **a less than 1% interest in the profits** of the partnership. (Section 6223(b)(1).)

73. However, if a group of partners in the aggregate having **a 5% or more interest in the profits** of a partnership so request and designate one of their members to receive the notice, the member so designated shall be treated as a partner entitled to such notices. (Section 6223(b)(2); Reg. 301.6223(b)-1(a).)

74. For purposes of the TEFRA rules in determining whether items are more appropriately determined at the partnership level, with respect to transactions to which Section

707(a) applies, the partnership must determine **the percentage of the capital interests and profits interests** in the partnership owned by each partner. (Reg. 301.6231(a)(3)-1(c)(4)(iii).)

75. For purposes of determining the tax matters partner if no general partner has been so designated, the general partner having **the largest profits interest** in the partnership at the close of such taxable year involved shall so act. (Section 6231(a)(7)(B); Reg. 301.6231(a)(7)-1(m)(2).)

76. For purposes of designating a tax matters partner for a partnership taxable year pursuant to Reg. 301.6231(a)(7)-1(e), a statement to be filed with the appropriate IRS service center shall be signed by the persons who were general partners at the close of the year and were shown on the return for that year to hold **more than 50% of the aggregate interest in partnership profits** held by all general partners as of the close of the taxable year. (Reg. 301.6231(a)(7)-1(e)(4).)

77. For purposes of designating a tax matters partner in a partnership taxable year pursuant to Reg. 301.6231(a)(7)-1(f), a statement to be filed with the appropriate IRS service center shall be signed by all persons who were partners at the close of the year and were shown on the return for that year to hold **more than 50% of the aggregate interest in partnership profits** held by all partners as of the close of the taxable year. (Reg. 301.6231(a)(7)-1(f)(2)(iv).)

78. For purposes of selecting the tax matters partner if no general partner may be selected (for reasons discussed in Reg. 301.6231(a)(7)-1(p)(2) or (3)(ii)), "the Commissioner may consider" six criteria including **"the profits interest held** by the partner" and "the views of the partners **having a majority interest** in the partnership." (Reg. 301.6231(a)(7)-1(q)(2)(iii) and (iv).)

79. For purposes of forming a "5% group" to file a petition for judicial review or appealing a judicial determination, a "5% group" is a group of partners who for the taxable year involved had **profits interests which aggregated 5% or more**. (Section 6231(a)(11).)

80. A partnership that has made a Section 444 election to use a tax year other than the tax year required under Section 706(b) must generally make a "required payment" under Section 7519 for any tax year in which the election is in effect. The computation of the required payment in turn requires, inter alia, the computation of the partnership's "applicable payments", which in general are any amounts deductible in the base year that are includible, directly or indirectly, in the gross income of a taxpayer that during the base year is a partner. An amount is "indirectly includible in the gross income of a partner" if the amount is includible in a partnership **more than 50% of the profits and capital** of which is owned in the aggregate by partners of the electing partnership. (Temp. Reg. 1.7519-1T(b)(5)(iv)(D)(1)(iii).)

81. For purposes of determining the applicable payments of an electing partnership, any amounts deducted by a "downstream controlled partnership" are considered deducted by the electing entity. If **more than 50% of the profits and capital interests** are owned by a partnership that has made a Section 444 election, such owned partnership is considered a "downstream controlled partnership". Furthermore, if **more than 50% of a partnership's profits and capital** are owned by a downstream controlled partnership, such owned partnership

also is considered a downstream controlled partnership. (Temp. Reg. 1.7519-1T(b)(5)(iv)(D)(2)(ii).)

82. In determining whether certain transfers are disregarded under Section 7704(b) in determining whether interests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof, transfers by one or more partners of **interests representing in the aggregate 50% or more of the total interests in partnership capital and profits** in one transaction or a series of related transactions are disregarded. (Reg. 1.7704-1(e)(1)(ix).)

83. For purposes of determining whether certain transfers are disregarded under Section 7704(b) in determining whether interests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof, the transfer by a partner and any related persons (as defined in Sections 267(b) and 707(b)(1)) in one or more transactions during any 30 calendar day period of partnership **interests representing in the aggregate more than 2% of the total interests in partnership capital or profits**. (Reg. 1.7704-1(e)(2).)

84. For purposes of determining whether certain transfers are disregarded under Section 7704(b) in determining whether interests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof, in determining whether the transfer of an interest in a partnership pursuant to a redemption or repurchase agreement is disregarded, one of the alternative tests requires that the sum of the percentage interests in partnership capital or profits transferred during the taxable year of the partnership (other than certain "private transfers") **does not exceed 10% of the total interests in partnership capital or profits**. (Reg. 1.7704-1(f)(3).)

85. For purposes of Section 7704(b), which disregards the transfer of an interest through a "qualified matching service" in determining whether interests in the partnership are readily tradable on a secondary market or the substantial equivalent thereof, the sum of the percentage interests in partnership capital or profits transferred during the taxable year of the partnership (other than certain "private transfers") **does not exceed 10% of the total interests in partnership capital or profits**. (Reg. 1.7704-1(g)(2)(viii).)

86. For purposes of Section 7704(b), interests in a partnership are not readily tradable on a secondary market or the substantial equivalent thereof if the sum of the percentage interests in partnership capital or profits transferred during the taxable year of the partnership (excluding certain specified categories of transfers) **does not exceed 2% of the total interests in partnership capital or profits**. (Reg. 1.7704-1(j).)

87. For purposes of Reg. 1.7704-1, in determining the total interests in partnership capital or profits, if the general partners and any person related to the general partners (within the meaning of Section 267(b) or 707(b)(1)) own, in the aggregate, **more than 10% of the outstanding interests in partnership capital or profits** at any one time during the taxable year of the partnership, the total interests in partnership capital or profits are determined without reference to the interests owned by such persons. (Reg. 1.7704-1(k)(1)(ii)(A).)

88. For purposes of rules relating to expatriated entities and their foreign parents under Section 7874, in determining an expanded affiliated group (EAG) that includes a foreign

corporation, for purposes of the ownership percentage determination stock held by one or more members of the EAG shall be included in the denominator (but not the numerator) of the fraction that determines the ownership percentage if, inter alia, (1) before the acquisition, **80% or more of the capital or profits interest** in the domestic entity was owned by the corporation that is the common parent of the EAG after the acquisition, and (2) after the acquisition, stock held by non-members of the EAG by reason of **holding a capital or profits interest in the domestic entity** does not exceed 20% of the stock of the foreign corporation. (Reg. 1.7874-1T(c)(1).)

89. For purposes of the rules relating to Section 7874, partnership interests owned by an entity in which **at least 50% of the capital or profits interest** is owned by the partnership in question shall not be taken into account for purposes of (1) determining the percentage of ownership of an entity under Reg. 1.7874-1T(c), or (2) treating stock held by one or more members of the EAG as included in the denominator (but not the numerator) under Reg. 1.7874-1T(c). (Reg. 1.7874-1T(d).)

90. For purposes of preparing the partnership tax return, Schedule K-1 calls for reporting **the percentage ownership of the partner in partnership capital and profits**.

91. For purposes of determining whether the filing of a new Schedule M-3 (Form 1065) to the partnership tax return is required, the determination of whether an entity is a "reportable entity partner" turns on whether the entity owns or is deemed to own **a 50% or greater interest in the partnership's income, loss or capital** on any day of the partnership's taxable year on or after June 30, 2006. (Form 1065, Schedule M-3 Draft Instructions, 6/27/06 Draft, "Reportable Entity Partner Reporting Responsibilities," pg. 2.) (Note: The 50% Ownership reference is with respect to the partnership's "capital, profit, or loss," on any day during the taxable year of the partnership," on Schedule M-3, Box D, and the Schedule M-3 Draft Instructions 2006, supra, "General Instructions – Who Must File," pg. 2.)

92. For purposes of determining whether the filing of a Schedule M-3 (Form 1065) to the partnership tax return is required, the owner of **50% or more of partnership income, loss or capital** on any day of the partnership tax year is deemed to own all corporate and partnership interests owned or deemed to be owned by the partnership during the partnership tax year. (Form 1065, Schedule M-3 Draft Instructions, 6/27/06 Draft, "Reportable Entity Partner Reporting Responsibilities," pg. 2.)

93. For purposes of preparing Schedule M-3 (Form 1065), for any tax year in which the partnership has more than two "reportable entity partners," the partnership must provide all of the information pertaining to Check Box D on page 1 of Schedule M-3 for the two reportable entity partners having the "maximum percentage of deemed ownership for the tax year of the partnership." The latter is defined as **the maximum percentage interest** deemed owned (under the Schedule M-3 Instructions) by the reportable entity partner **in the partnership's capital, profit, or loss** on any day during the partnership's taxable year. (Form 1065, Schedule M-3 Draft Instructions, 6/27/06 Draft, "Reportable Entity Partner Reporting Responsibilities," pg. 3.)

[MORE TO COME]

APPENDIX II
DERIVATIVE REFERENCES (INCORPORATING PIPP AND PIPC)
UNDER 267(b) AND/OR 707(b)

1. For purposes of determining the availability of low-income housing tax credits under Section 42 for existing buildings, the existing building must be acquired by "purchase" as defined in Section 179(d), which excludes, among other things, acquisitions from a person whose relationship to the acquiring person would result in disallowance of losses under Section **267 or 707(b), utilizing a 10% threshold** instead of 50%. (Section 42(d)(2)(D)(iii)(I)).

2. For purposes of determining the availability of low-income housing tax credits under Section 42 for existing buildings, the existing building must not have been previously placed in service by any person who was related to the taxpayer as of the time previously placed in service, where (among other things) the relationship is as specified in Section **707(b)(1), utilizing a 10% threshold** instead of 50%. (Section 42(d)(2)(D)(iii)(II)).

3. A low-income building can utilize a credit allocation from a prior year in certain circumstances, which include a requirement that the basis in the low-income housing project at specified times is more than 10% of the taxpayer's reasonably expected basis in such project. For purposes of this determination, certain fees may be included in basis, for which purpose one of the requirements is that the fee be paid (or to be paid) to a related person be accounted for under the accrual method, where the related person must bear a relationship to the taxpayer specified in Section **267(b) or 707(b)(1)** or be engaged in a trade or business under common control with the taxpayer. (Section 1.42-6(b)(2)(iv)(E)).

4. For purposes of allocating the new markets tax credit under Section 45D, the Secretary is directed to give priority to any entity that (among other things) intends to make "qualified low-income community investments" in one or more businesses in which persons unrelated to such entity (within the meaning of **267(b) or 707(b)(1)(B)**) hold the majority equity interest. (Section 45D(f)(2)(B)).

5. Sections 83(a) and 83(b) apply to the transfer of money or other property received if an option is sold or otherwise disposed of in an arm's length transaction in the same manner as sections 83(a) and 83(b) would have applied to the transfer of property pursuant to an exercise of the option unless the sale or other disposition of the option is to a person related to the service provider and occurs on or after July 2, 2003, where a person will be treated as related (among others) if the person and the service provider bear a relationship to each other specified in section **267(b) or 707(b)(1), utilizing 20%** instead of 50%. (Section 1.83-7(a)(1)).

6. For purposes of the rule limiting the exclusion from gross income of an applicable policyholder as to employer-owned life insurance, "applicable policyholder" includes any person which bears a relationship which is specified in section **267(b) or 707(b)(1)** to the person that owns the life insurance contract, is engaged in a trade or business, and is directly or indirectly a beneficiary of the contract. (Section 101(j)(3)(B)(ii)(I)).

7. Discharge of indebtedness income is created when a taxpayer's debt is acquired at a discount by a related person, defined as including a person related under Section **267(b) or 707(b)(1)**. (Section 108(e)(4).)

8. The exclusion for certain gains on the sale of a principal residence can apply to sales or exchanges of remainder interests in the residence unless the sale or exchange is with a person who bears a relationship to the taxpayer which is described in section **267(b) or 707(b)**. (Section 121(d)(8)(B)).

9. In determining whether a bond qualifies as a "qualified small issue bond," certain issues will be aggregated based, in part, on whether the facilities financed will be used by the same person or 2 or more persons that bear such a relationship that would result in a disallowance of losses under section **267 or 707(b)**. (Sections 144(a)(3) as implemented by 144(a)(2)(B), 144(a)(4)(B)(ii), 144(a)(6)(A)(ii), 144(a)(6)(B) and 144(a)(10)(E)).

10. In determining whether a bond qualifies as a "qualified small issue bond," issues where more than $250,000 of the net proceeds are used to provide depreciable farm property where the principal user is or will be the same person or 2 or more persons that bear such a relationship that would result in a disallowance of losses under section **267 or 707(b)**. (Sections 144(a)(3) as implemented by 144(a)(11)(A)).

11. In determining whether a bond qualifies as a "qualified redevelopment bond," the bond must be used for 1 or more redevelopment purposes in a designated blighted area, which must may be a contiguous area equaling or exceeding 10 acres if not more than 25% of the financed area is to be provided to one person, treating all persons that bear such a relationship that would result in a disallowance of losses under section **267 or 707(b)** as one person. (Section 144(c)(4)(D)(ii)).

12. A private activity bond is not a qualified bond if it is held by a person who is a substantial user of the facilities or by a related person of such a substantial user, where a related person includes (among others) 2 or more persons if the relationship between such persons would result in a disallowance of losses under section **267 or 707(b)**. (Section 147(a)(2)(A)).

13. In certain situations, OID on a debt instrument held by a related foreign person may not be deducted until paid, for purposes of which a "related foreign person" is any person who is not a U.S. person and who is related (within the meaning of Section **267(b))** to the issuer. (Section 163(e)(3)(C)).

14. The interest stripping rules of Section 163(j) may disallow the interest deduction for interest paid or accrued by a taxpayer (directly or indirectly) to a related person if no federal income tax is imposed on such interest, interest paid or accrued by a taxpayer with respect to any indebtedness to a person who is not a related person if there is a disqualified guarantee of such indebtedness and no gross basis tax is imposed on such interest and interest paid or accrued by a taxable REIT subsidiary of a REIT to the REIT. For these purposes, a "related person" in general is any person who is related within the meaning of **267(b) or 707(b)(1)** to the taxpayer, except that interest paid or accrued to a partnership which would be a related person (but for the exception) will not be treated as paid or accrued to a related person if less than 10% of the profits

and capital interests in such partnership are held by persons with respect to whom no federal income taxes are imposed on such interest (with a further exception that the exception does not apply to interest allocable to any partner of such partnership who is a related person to the taxpayer). (Section 163(j)(4)(A)).

15. With certain exceptions, an interest deduction is not allowed for interest on any indebtedness of a corporation payable in equity of the issuer or a related party or equity held by the issuer (or a related party) in any other person, where a "related party" includes a person that bears a relationship to the issuer described in Section **267(b) or 707(b)**. (Section 163(l)(6)).

16. A theft loss is allowed for losses reasonably estimated to have occurred on a qualified individual's deposit in a qualified institution that went bankrupt or became insolvent. For purposes of this provision, "qualified individual" means an individual except an individual that owns at least 1% of the institution, is an officer of the institution, who has certain familial ties to such an owner or officer or who otherwise is a related person (as defined in Section **267(b)**) with respect to such an owner or officer. (Section 165(l)(2)).

17. No Section 167 depreciation is allowed to the taxpayer for any term interest in property for any period during which the remainder interest in such property is held (directly or indirectly) by a related person, which means any person bearing a relationship to the taxpayer described in subsection **(b)** or (e) of Section **267**. (Section 167(e)(5)(B)).

18. For purposes of calculating Section 167 depreciation on the income forecast method or any other similar method, in the case of television and motion picture films, the income from the property shall include income from the exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent that such income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related persons (within the meaning of Section **267(b)**) to the taxpayer. (Section 167(g)(5)(C)).

19. If public utility property is acquired in a carryover basis transaction or in a transfer from a related person, then the applicable 1968 method with respect to such property shall be determined by reference to the treatment in respect of such property in the hands of the transferor. For this purpose, a related person is any person that is related to another if either immediately before or after the transfer the persons are members of the same controlled group or the relationship would result in a disallowance of losses under Section **267 or 707(b)**. (Section 1.167(l)-1(e)(4)(ii)(b)(1)).

20. The bonus depreciation provided in Section 168(k) for property placed in service after September 10, 2001 and before January 1, 2005 was only available for "qualified property," which did not include property if the user of the property (on the date of original placement in service) or a person related (within the meaning of Section **267(b) or 707(b)**) to such user or the taxpayer had a written contract in effect for the acquisition of the property at any time on or before September 10, 2001. (Section 168(k)(2)(E)(iv)(I)).

21. For purposes of bonus depreciation, if, in the ordinary course of its business, a taxpayer sells fractional interests in property to unrelated third parties, each first fractional owner

of the property is considered as the original user of its proportionate share of the property and if the taxpayer uses the property before all of the fractional interests of the property are sold but the property continues to be held primarily for sale by the taxpayer, the original use of any fractional interest sold to an unrelated third party subsequent to the taxpayer's use of the property begins with the first purchaser of that fractional interest, for purposes of which persons are not related if they do not have a relationship described in section **267(b) or 707(b)**. (Section 1.168(k)-1T(b)(3)(iv)).

22. Among other exclusions and with certain additional related rules, Section 1245 property and Section 1250 property acquired by the taxpayer after December 31, 1980 will not qualify for ACRS if the property was owned or used at any time during 1980 by the taxpayer or a related person or the property is leased by the taxpayer for more than 3 months to a person (or a person related to such person) who owned or used such property at any time during 1980, in each case where the relationship specified in Section **267(b) or 707(b)(1), utilizing 10%** instead of 50% will cause two persons to be related. (Section 1.168-4(d)(6)).

23. The rules of Section 1.168(h)-1 apply with respect to a direct or indirect transfer of property among related persons if Section 1031 applied to any party to the transfer or to any related transaction and if a principal purpose of the transfer or related transaction is to avoid or limit the application of the alternative depreciation system, for purposes of which a person will be treated as related to another if they bear a relationship specified in section **267(b)** or section **707(b)(1)**. (Section 1.168(h)-1).

24. Charitable contributions of future interests in personal tangible property are treated as made only when all intervening interests in, and rights to the actual possession or enjoyment of, the property have expired or are held by persons other than the taxpayer or those standing in the relationship to the taxpayer described in Section **267(b) or 707(b)**. (Section 170(a)(3)).

25. To satisfy the substantiation requirements for certain charitable contributions, it is necessary to obtain a qualified appraisal, which must be prepared, signed, and dated by a qualified appraiser. A qualified appraiser does not include (among others) any person related under Section **267(b)** to or married to a person who is in a relationship described in Section **267(b)** with the donor, the taxpayer claiming the deduction, a party to the transaction in which the donor acquired the property, the donee or an employee of any of these person. (Section 1.170A-13(c)(5)(iv)(E)).

26. Contributions of conservation easements where a mineral interest is retained does not qualify for a charitable contribution deduction if the minerals may be extracted by any surface mining method unless (among other things) the present owner of the mineral interest is not a person whose relationship to the owner of the surface estate is described at the time of the contribution in section **267(b)** or section **707(b)**. (Section 1.170A-14(g)(4)(ii)(A)(2)).

27. For purposes of determining the value of contribution of a conservation easement, the deduction may be disallowed or reduced if the donor or a related person receives, or can reasonably expect to receive, financial or economic benefits, for purposes of which related

person has the same meaning as in either section **267(b)** or section **707(b)**. (Section 1.170A-14(h)(3)(i)).

28. A "convertible bond" for purposes of applying a rule regarding the determination of a holder's basis in a convertible bond is a bond that provides the holder with an option to convert the bond into stock of the issuer, stock or debt of a related party (within the meaning of section **267(b) or 707(b)(1)**), or into cash or other property in an amount equal to the approximate value of such stock or debt. (Section 1.171-1(e)(1)(iii)(C)).

29. The deduction available for Section 179 property, which (among other things) must be acquired by purchase for use in the active conduct of a trade or business, where "purchase" does not include acquisitions from persons whose relationship to the acquiring person would result in disallowance of losses under Section **267 or 707(b)**. (Section 179(d)(2)).

30. Taxpayers (and their related persons) may not deduct more than $100,000, over the years, in qualified clean-fuel vehicle refueling property, where "related persons" include persons who bear a relationship described in Section **267(b) or 707(b)(1)**. (Section 179A(b)(2)(B)).

31. The anti-churning rules as to amortization of section 197 intangibles applies (among others) to those intangibles that were held or used at any time on or after July 25, 1991 and on or before July 25, 1991 by the taxpayer or a related person or if the taxpayer grants the right to use the intangible to a person (or a person related to such person) who held or used such intangible at any time on or after July 25, 1991 and on or before July 25, 1991, in each case where the related person bear a relationship described in Section **267(b) or 707(b)(1), utilizing 20%** instead of 50%, immediately before or immediately after the acquisition of the intangible involved. (Section 197(f)(9)(C)).

32. For purposes of the trade-or-business rules in Treas. Reg. 1.197-2(e), assets will only be considered acquired if they are acquired by the taxpayer and persons related to the taxpayer from another person and persons related to that other person, in each case treating two persons as related only if their relationship is described in section **267(b) or 707(b)** or they are engaged in trades or businesses under common control within the meaning of section 41(f)(1). (Section 1.197-2(e)(3)).

33. Amounts paid for qualified long-term care services provided to an individual is not treated as paid for medical care (for purposes of the Section 213 deduction) if such services is provided by an unlicensed spouse or relative or by a corporation or partnership which is related (within the meaning of Section **267(b) or 707(b)**) to the individual. (Section 213(d)(11)(B)).

34. The deduction for interest on education loans is not available on indebtedness owed to a person who is related (within the meaning of Section **267(b) or 707(b)(1)**) to the taxpayer. (Section 221(d)(1)).

35. For purposes of determining if a holding period should be shortened by reason of positions that result in a diminished risk of loss, positions held by a party related to the taxpayer within the meaning of Sections **267(b) or 707(b)(1)** are treated as positions held by the taxpayer

if the positions are held with a view to avoiding the application of Section 246 or Treas. Reg. 1.1092(d)-2. (Section 1.246-5(c)(6)).

36. For purposes of Section 263(a) requiring capitalization of certain expenditures, references to a party other than the taxpayer include persons related to that party and persons acting for or on behalf of that party (including persons to whom the taxpayer becomes obligated as a result of assuming a liability of that party), for purposes of which persons are related only if their relationship is described in Section **267(b) or 707(b)** or they are engaged in trades or businesses under common control within the meaning of section 41(f)(1). (Section 1.263(a)-4 and -5).

37. A small reseller is not required to capitalize additional Section 263A costs to personal property produced for it under contract with an unrelated person and may use the simplified resale method if the contract is entered into incident to the resale activities of the small reseller and the property is sold to its customers, for purposes of which persons are related if they are described in Section **267(b) or 707(b)**. (Section 1.263A-3(a)(3) and -3(a)(4)(iii)).

38. Distribution costs, which are not generally required to be capitalized, do not include costs incurred by a taxpayer in delivering goods to a related person and, when a taxpayer sells goods to a related person, the costs of transporting the goods are included in determining the basis of the goods that are sold, and hence in determining the resulting gain or loss from the sale, for purposes of which persons are related if they are described in Section **267(b)** or section **707(b)**. (Section 1.263A-3(c)(4)(vi)(A)(2)).

39. For purposes of Treas. Regs. 1.263A-8 through 1.263A-15 (dealing with capitalization requirements as to certain expenditures, including interest), a person is related to a taxpayer if their relationship is described in section **267(b) or 707(b)**. (Section 1.263A-8(a)(4)(i)).

40. If, pursuant to the matching and acceleration rules of Treas. Reg. 1.1502-13(c) and (d) as implemented by Section 1.267(f)-1(c)), a member of a controlled group that sold property to another member of that controlled group takes into account a loss or deduction as a result of the other member's transfer of the property to a nonmember that is a person related to any member, immediately after the transfer, under Sections **267(b) or 707(b)** (among other times), the loss or deduction is taken into account but allowed only to the extent of any income or gain taken into account as a result of the transfer. (Section 1.267(f)-1(c)(1)(iii)).

41. For purposes of determining whether a foreign corporation is a stapled foreign corporation, the Commissioner may, at his discretion, treat interests that otherwise would be stapled interests as not being stapled if the same person or related persons (within the meaning of Section **267(b) or 707(b)**) hold stapled interests constituting more than 50 percent of the beneficial ownership of both corporations, and a principal purpose of the stapling of those interests is the avoidance of U.S. income tax. (Section 1.269B-1(b)(2)).

42. In determining the extent to which Section 274(e)(2) will limit an entertainment expense deduction, individuals who are subject to the requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to the taxpayer or a related person to the taxpayer

or would be so subject if the taxpayer (or such related person) were an issuer of equity securities referenced in section 16(a), where "related person" includes persons that bear a relationship described in Section **267(b) or 707(b)**. (Section 274(e)(2)(B)(ii)).

43. For purposes of determining the portion of travel that will be allocable to business activity in determining the portion of the travel expenses that may be deducted, any individual who travels on behalf of his employer under a reimbursement or other expense allowance arrangement shall be considered not to have had substantial control over the arranging of his business trip and thus to have such trip fully allocable to business activity, provided the employee is not (among others) related to his employer within the meaning of Section **267(b)**, but for this purpose the percentage referred to in Section 267(b)(2) shall be 10 percent. (Section 1.274-4(f)(5)(i)(b)).

44. For purposes of determining the amount of qualified business use to determine whether Section 280F will act to limit or deny deductions for lease payments or depreciation, certain uses by certain persons cannot be included. For this purpose, "related person" means any person related to the taxpayer (within the meaning of Section **267(b)**). (Section 280F(d)(6)(D)(ii)).

45. In a Section 304 acquisition where the acquiring corporation is a foreign corporation, the only earnings and profit taken into account for purposes of Section 304(b)(2)(A) are those which are attributable to stock owned by a corporation which is a U.S. shareholder of the acquiring corporation for purposes of subpart F and the transferor (or a person who bears a relationship to the transferor described in Section **267(b) or 707(b)**) and which were accumulated during the period such stock was owned by such person while the acquiring corporation was a CFC. (Section 304(b)(5)(A)).

46. The rule specifying that where a corporation that issues preferred stock, which may be redeemed under certain circumstances at a price higher than the issue price, the difference (the redemption premium) is treated under Section 305(c) as a constructive distribution (or series of constructive distributions) of additional stock on preferred stock that is taken into account under principles similar to the principles of Section 1272(a) will not apply if (among other considerations) the issuer's obligation to redeem or the holder's ability to require the issuer to redeem is subject to a contingency that is beyond the legal or practical control of either the holder or the holders as a group (or through a related party within the meaning of Section **267(b) or 707(b)**), and that, based on all of the facts and circumstances as of the issued date, renders remote the likelihood of redemption. (Section 1.305-5(b)(2)).

47. The rule described in #47 above will apply if the issuer has the right to redeem the stock but only if, based on all of the facts and circumstances as of the issue date, redemption pursuant to that right is more likely than not to occur. A redemption pursuant to an issuer's right to redeem is not treated as more likely than not to occur if (among other things) the issuer and the holder are not related within the meaning of Section **267(b) or 707(b), utilizing 20%** instead of 50%. (Section 1.305-5(b)(3)(ii)(A)).

48. For purposes of the consistency rules under Section 338(e) and (f), the consistency period is extended to include any continuous period that ends on, or begins on, any

day of the consistency period during which a purchasing corporation, or any person related, within the meaning of Section **267(b) or 707(b)(1)**, to a purchasing corporation, has an arrangement to purchase stock of target or to own an asset to which the carryover basis rules of Section 1.338-8 apply, taking into account the extension. (Section 1.338-8(j)(1)).

49. The 12-month acquisition period, for purposes of determining whether a qualified stock purchase has been made, is extended if, pursuant to an arrangement, a corporation acquires by purchase stock of another corporation satisfying the requirements of section 1504(a)(2) over a period of more than 12 months. For purposes of determining whether an arrangement exists, one factor considered is the participation of a person related within the meaning of Section **267(b) or 707(b)(1)**. (Section 1.338-8(j)(5)).

50. Preferred stock is nonqualified preferred stock under Section 351(g) if the holder has the right to require the issuer or a related person to redeem or purchase the stock, the issuer or a related person is required to redeem or purchase such stock, the issuer or a related person has the right to redeem or purchase the stock in certain circumstances, or the dividend rate varies in whole or part (directly or indirectly) with reference to certain types of indices. In each case, a person is related to another person if they bear a relationship to such other person described in Section **267(b) or 707(b)**. (Section 351(g)(3)(B)).

51. For purposes of applying the rules of Section 355(d), which provides that a spin-off is disqualified if, after the spin-off, any person owns 50% or more of the stock of either the distributing or controlled corporation and that stock is so-called "disqualified stock," a person and all persons related to such person (within the meaning of Section **267(b) or 707(b)(1)**) are treated as one person. (Section 355(d)(7)(A)).

52. The exception to the disqualified investment company rules of Section 355(g) for investment assets used in the active conduct of lending or finance businesses, banking businesses or insurance businesses only applies if substantially all of the income of the business is derived from persons who are not related (within the meaning of Section **267(b) or 707(b)(1)**) to the person conducting the business. (Section 355(g)(2)(B)(ii)).

53. Where there is a later direct or indirect disposition of intangible property transferred under circumstances triggering Section 367(d), in general, deemed annual license payments will continue if a transfer is made to a related person, while gain must be recognized immediately if the transfer is to an unrelated person, for purposes of which persons are considered related if they are partners or partnerships described in section **707(b)(1)** of the Code. (Section 1.367(d)-1(h)(1)).

54. For purposes of determining whether an ownership change occurs, an option is treated as exercised on the date of its issuance or transfer if, on that date, the option satisfies three tests, one of which (the control test) requires (among other things) the holder of the option and any persons related to the option holder have, in the aggregate, a direct and indirect ownership interest in the loss corporation of more than 50 percent, treating persons as related if they bear a relationship specified in Section **267(b) or 707(b)** or if they have a formal or informal understanding among themselves to make a coordinated acquisition of stock, within the meaning of Treas. Reg. 1.382-3(a)(1)(i). (Section 1.382-4(d)(4)(ii)(A)(2)).

55. For purposes of determining whether indebtedness is qualified indebtedness under Section 382(l)(5), indebtedness ownership periods will tack in certain circumstances, including upon transfers between parties who bear a relationship to each other described in Section **267(b) or 707(b)**, **utilizing 80%** instead of 50%. (Section 1.382-9(d)(5)(ii)(A)).

56. A plan to which Section 1042 applies and an eligible worker-owned cooperative (within the meaning of Section 1042(c)) shall provide that no portion of the assets of the plan or cooperative attributable to (or allocable in lieu of) employer securities acquired by the plan or cooperative in a sale to which Section 1042 applies may accrue (or be allocated directly or indirectly under any plan of the employer meeting the requirements of section 401(a)) during the nonallocation period, for the benefit of (among others) any individual who is related to the taxpayer (within the meaning of Section **267(b)**). (Section 409(n)(1)(A)(ii)).

57. Section 409A does not apply to an amount deferred under an arrangement between a service provider and service recipient with respect to a particular trade or business in which the service provider participates, if during the service provider's taxable year in which the service provider obtains a legally binding right to the payment of the amount deferred the service provider is actively engaged in the trade or business of providing services, other than as an employee or as a director of a corporation, service provider provides significant services to two or more service recipients to which the service provider is not related and that are not related to one another (for purposes of which persons are related if they bear a relationship specified in Section **267(b) or 707(b)(1), utilizing 20%** instead of 50%) and service provider is not related to the service recipient (for purposes of which persons are related if they bear a relationship specified in Section **267(b) or 707(b)(1)**, without the aforementioned modification). For purposes of the "significant services" portion of the foregoing, a service provider who provides services to two or more service recipients to which the service provider is not related and that are not related to one another (for purposes of which persons are related if they bear a relationship specified in Section **267(b) or 707(b)(1), utilizing 20%** instead of 50%) is deemed to be providing significant services to two or more of such service recipients for a given taxable year, if the revenues generated from the services provided to any service recipient or group of related service recipients during such taxable year do not exceed 70 percent of the total revenue generated by the service provider from the trade or business of providing such services. (Proposed Section 1.409A-1(f)(3)).

58. A notional principal contract definitionally requires payments calculated by reference to a specified index, which includes an interest rate index that is regularly used in normal lending transactions between a party to the contract and unrelated persons. If a taxpayer, either directly or through a related person, reduces risk with respect to a notional principal contract by purchasing, selling, or otherwise entering into other notional principal contracts, futures, forwards, options, or other financial contracts (other than debt instruments), the taxpayer may not use the alternative methods provided in Treas. Reg. 1.446-3(f)(2)(iii) and (v). There is also a consistency rule regarding estimations of a specified index among the taxpayer and parties related to the taxpayer that are parties to the notional principal contract. For purposes of these rules, A related person is a person related (within the meaning of Section **267(b) or 707(b)(1)**) to one of the parties to the notional principal contract or a member of the same consolidated group (as defined in Treas. Reg. 1.1502-1(h)) as one of the parties to the contract. (Section 1.446-3(c)(4)(i)).

59. The installment sale rules do not apply to transfers of depreciable property to related persons, where related persons includes 2 or more partnerships having a relationship to each other described in Section **707(b)(1)(B)**. (Section 453(g)(3)).

60. For purposes of the rules relating to accounting for long-term contracts (including, for example, determining the contract commencement date), a related party is a person whose relationship to a taxpayer is described in Section **707(b) or 267(b)**, with certain modifications relevant to Section 267(b) only. (Section 1.460-1(b)(4)).

61. To obtain a deduction in the year of payment on a contested, asserted liability, the payment must satisfy certain requirements. Payment to a person (other than the person asserting the liability) of any stock of the taxpayer or of any stock or indebtedness of a person related to the taxpayer (as defined in Section **267(b)**) will not qualify. (Section 1.461-2(c)(1)(iii)(E)).

62. Amounts borrowed from any person who has an interest in an activity or from a related person to a person (other than the taxpayer) having such an interest are not considered at risk with respect to an activity, where "related person" includes persons bearing a relationship specified in Section **267(b) or 707(b)(1), utilizing 10%** instead of 50%. (Section 465(b)(3)(C)).

63. For purposes of determining the amount that a taxpayer has at-risk in an activity, amounts which are borrowed from (among others) a person with a relationship to the taxpayer specified within any one of the paragraphs of section **267(b)** shall be treated in the same manner as amounts borrowed for which the taxpayer has no personal liability and for which no security is pledged. (Proposed Section 1.465-20(a)(2)).

64. Except for purposes of determining whether a section 467 rental agreement is a leaseback within the meaning of Treas. Reg. 1.467-3(b)(2), two persons are related persons for purposes of regulations under Section 467 if they either have a relationship to each other that is specified in Section **267(b) or 707(b)(1)** or are related entities within the meaning of Sections 168(h)(4)(A), (B), or (C). (Section 1.467-1(h)(11)).

65. For purposes of determining whether a payment is a qualified payment and whether a fund is a designated settlement fund in Section 468B, certain rules reference related persons. For example, as to qualified payments, amounts which may be transferred to the taxpayer or any related person or transfers of stock or indebtedness of the taxpayer or any related person will not qualify. As to designated settlement funds, among other things, the fund must be established for the principal purpose of resolving and satisfying present and future claims against the taxpayer (or any related person or formerly related person) arising out of personal injury, death, or property damage and, under the terms of the fund, the taxpayer (or any related person) may not hold any beneficial interest in the income or corpus of the fund. For these purposes, a "related person" means a person related to the taxpayer within the meaning of Section **267(b)**. (Section 468(d)(3)).

66. For purposes of the segregation requirement as to qualified settlement funds under Treas. Reg. 1.468B-1(c)(3) and (h), a related person is any person who is related to the transferor within the meaning of Sections **267(b) or 707(b)(1)**. (Section 1.468B-1(d)(2)).

67. Providing debt of a related person (within the meaning of Section **267(b) or 707(b)(1)**) does not constitute economic performance (which is delayed until principal payments are made on such debt), despite the rules providing that a transfer to a disputed ownership fund to resolve or satisfy a liability will constitute such economic performance. (Section 1.468B-9(d)(2)(ii)).

68. Passive activity losses may be deducted in the taxable year in which a taxpayer disposes of his entire interest in the passive activity in a taxable transaction unless the acquiring party and the taxpayer bear a relationship to each other described in Section **267(b) or 707(b)(1)**, in which case the loss may only be deducted in the taxable year in which such interest is so acquired by another person who does not bear such relationship to the taxpayer. (Section 469(g)(1)(B)).

69. Except as otherwise provided in Treas. Reg. 1.469-4T(j)(3)(iii)(B), a person's ownership percentage in a pass-through entity or in an undertaking shall be determined by treating such person as the owner of any interest that a person related to such person owns (determined without regard to Treas. Reg. 1.469-4T(j)(3)(iii)) in such pass-through entity or in such undertaking, treating persons as related if the relationship of such persons is described in section **267(b) or 707(b)(1)**. (Section 1.469-4T(j)(3)(iii)(C)).

70. To determine whether the mark-to-market accounting method is available, the taxpayer must be a dealer in securities, where securities includes notes, bonds, debentures or other evidences of indebtedness and such terms do not include nonfinancial customer paper. Nonfinancial customer paper is a receivable which is a note, bond, debenture or other evidence of indebtedness, arises from the sale of nonfinancial goods or services by a person the principal activity of which is selling or providing such goods or services and is held by such person (or a person who bears a relationship to such person described in Section **267(b) or 707(b)**) at all times since issue. (Section 475(c)(4)(B)(iii)).

71. A partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust, to which the taxpayer has a relationship described in Section **707(b)(1)(A) or (B)** held by a dealer in securities are per se held for investment within the meaning of Section 475(b)(1)(A) and are deemed to be properly identified as such for purposes of Section 475(b)(2). (Section 1.475(b)-1(b)(i)).

72. Gains or losses from certain sales, exchanges or other dispositions of certain Brownfield properties are not unrelated business taxable income. In particular, the Brownfield property must be acquired from an unrelated person and must be sold, exchanged or disposed of to an unrelated person. In both cases, a person is treated as related if such person bears a relationship to such other person described in Section **267(b)** (with one exception) **or 707(b)(1), utilizing 25%** instead of 50% with an additional requirement if such other person is a nonprofit organization. (Section 512(b)(19)(J)).

73. While "acquisition indebtedness" for purposes of the unrelated business income tax does not generally include indebtedness to acquire or improve real property, this exception to the definition of "acquisition indebtedness" does not apply (among other times) if the real property is at any time after the acquisition leased to any person that bears a relationship

described in Section **267(b) or 707(b)** to the person selling the property to the qualified organization. (Section 514(c)(9)(B)(iii)).

74. If a corporation acquires the assets of a large bank (among other ways) in any direct or indirect acquisition of a significant portion of a large bank's assets if, after the acquisition, the transferor large bank owns more than 50 percent (by vote or value) of the outstanding stock of the acquirer, the acquiring corporation (the acquiror) is treated as a large bank for any taxable year ending after the date of the acquisition in which it is an institution described in Treas. Reg. 1.585-1(b)(1)(i) or (ii). For purposes of the foregoing test, stock of the acquirer is treated as owned by a transferor bank if the stock is owned by (among others) any related party within the meaning of Section **267(b) or 707(b)**. The acquirer is treated as a large bank, under the foregoing rule, if the acquisition is any direct or indirect acquisition of substantially all of a large bank's assets if the transferor large bank and the acquiror are related parties (within the meaning of Section **267(b) or 707(b)**) before or after the acquisition and a principal purpose of the acquisition is to avoid treating the acquired assets as those of a large bank. (Section 1.585-5(b)(2)).

75. In determining the maximum amount of depletion a taxpayer may take under 613A, the depletable oil quantity is must be allocated among corporations, trusts and estates owned by the same or related persons, where related persons includes persons that bear a relationship that would result in disallowance of losses under Section **267 or 707(b)**. (Section 613A(c)(8)(D)(ii)).

76. The rule allowing certain transfers of coal or iron ore to be treated as a gain or loss on the sale of the coal or iron ore does not apply to disposals to a person whose relationship to the disposing person would result in disallowance of losses under Section **267 or 707(b)**. (Section 631(c)).

77. Section 643(i), which deems certain loans of cash or marketable securities by foreign trusts to be distributions by such trust to the grantor or beneficiary, only applies to loans directly or indirectly to any U.S. grantor or beneficiary or to any U.S. person that is related to a U.S. grantor or beneficiary, where the relationship between the U.S. person and the U.S. grantor or beneficiary would result in disallowance of losses under Section **267 or 707(b)**. (Section 643(i)(2)(B)(i)).

78. For purposes of Reg. 1.643(h)-1, relating to distributions by certain foreign trusts through intermediaries, a United States person is treated as related to a grantor of a foreign trust if the United States person and the grantor are "related" for purposes of section 643(i)(2)(B), while for purposes of Section **267 and 707(b)(1) utilizing "at least 10%**" instead of "more than 50%." (Section 1.643(h)-1(e)).

79. For purposes of determining whether a "qualified gratuitous transfer" has occurred under the rules for charitable remainder trusts, if any portion of the assets of an ESOP attributable to securities acquired by the ESOP in a qualified gratuitous transfer are allocated to the account of (among others) any person who is related to the decedent (within the meaning of Section **267(b)**), the ESOP shall be treated as having distributed (at the time of such allocation) to such person or shareholder the amount so allocated. (Section 664(g)(5)).

80. A transfer by a U.S. person to a foreign trust through an intermediary will be treated as an indirect transfer by that U.S. person to the foreign trust if such transfer is made pursuant to a plan one of the principal purposes of which is the avoidance of United States tax, which will be deemed to exist if (among other things) the U.S. person is "related" to a beneficiary of the foreign trust, or has another relationship with a beneficiary of the foreign trust that establishes a reasonable basis for concluding that the U.S. transferor would make a transfer to the foreign trust, where such relationship meets the requirements of Section 643(i)(2)(B), while for purposes of Section **267 and 707(b)(1) utilizing "at least 10%"** instead of "more than 50%." (Section 1.679-3(c)).

81. The term "qualified funeral trust" does not include any trust (treating all trusts having trustees that are related persons as one trust) which accepts aggregate contributions by or for the benefit of an individual in excess of $7,000. For purposes of this test, related persons include persons whose relationship is described in Section **267 or 707(b)**. (Section 685(c)(2)(A)).

82. The deficit-restoration-obligation and liquidation-in-accordance-with-positive-capital-account-balances requirements for the economic effect safe harbor under Section 704(b) are not violated if all or part of the partnership interest of one or more partners is purchased (other than in connection with the liquidation of the partnership) by the partnership or by one or more partners (or one or more persons related, within the meaning of section **267(b)** (without modification by section 267(e)(1)) **or** section **707(b)(1)**, to a partner) pursuant to an agreement negotiated at arm's length by persons who at the time such agreement is entered into have materially adverse interests and if a principal purpose of such purchase and sale is not to avoid the fundamental principles of the economic effect safe harbor. (Section 1.704-1(b)(2)(ii)(b)).

83. For purposes of the Section 704(b) regulations, the partnership agreement includes agreements with a person related, within the meaning of section **267(b)** (without modification by section 267(e)(1)) **or** section **707(b)(1)**, to such partner or partnership, **utilizing "80 percent or more"** instead of "more than 50 percent". (Section 1.704-1(b)(2)(ii)(h)).

84. The transition rule, which allows partnerships to apply the provisions of Treas. Reg. 1.704-1(b) as if they had not been amended regarding the allocations of foreign tax expenditures if the partnership agreement was entered into before April 21, 2004 until any subsequent material modification to the partnership agreement occurs, does not apply if, as of April 20, 2004, persons that are related to each other (within the meaning of section **267(b) and 707(b)**) collectively have the power to amend the partnership agreement without the consent of any unrelated party. (Section 1.704-1T(b)(1)(ii)(b)(2)).

85. Interests of disregarded foreign partners are not ignored for purposes of determining a partnership's taxable year if each partner that is not a disregarded foreign partner (a "regarded partner") holds less than a 10% interest, and the regarded partners, in the aggregate, hold less than a 20% interest in the capital or profits of the partnership, treating each regarded partner as owning any interest in the partnership owned by partners that are related within the meaning of sections **267(b) or 707(b), utilizing "10%"** instead of "50%". (Section 1.706-1(b)(6)(iii)).

86. For purposes of the disguised sale of partnership interest rules under Section 707(a)(2)(B), an increase in a partner's share of a partnership liability may be treated as a transfer of consideration by the partner to the partnership, notwithstanding any other rule in Treas. Reg. 1.707-7, if within a short period of time after the partnership incurs or assumes the liability or another liability, one or more partners of the partnership, or related parties to a partner (within the meaning of section **267(b) or 707(b)**), in substance bears an economic risk for the liability that is disproportionate to the partner's interest in partnership profits or capital; and the transactions are undertaken pursuant to a plan that has as one of its principal purposes minimizing the extent to which the partner is treated as making a transfer of consideration to the partnership that may be treated as part of a disguised sale of partnership interests. (Proposed Section 1.707-7(j)(8)).

87. For purposes of the allocation of liabilities among partners under Section 752, a person is related to a partner if the person and the partner bear a relationship to each other that is specified in section **267(b) or 707(b)(1), utilizing "80 percent or more"** instead of "more than 50 percent" and with certain additional rules where a person is related to more than one partner. (Section 1.752-4(b)(1)).

88. Basis adjustments as the result of Section 734(b) may not be made to stock of a corporation if that corporation is a partner of the partnership in which the basis adjustment is being made or if a person related to the corporation is a partner in that partnership, where the related person has a relationship with the corporation described in Section **267(b) or 707(b)(1)**. (Section 755(c)).

89. For purposes of determining whether a segregated asset account that is a real property account is adequately diversified during its start-up period to obtain annuity, endowment, or life insurance contract treatment, amounts transferred to the account from a diversified account (determined without regard to this rule) or as a result of an exchange pursuant to Section 1035 in which the issuer of the contract received in the exchange is not related in a manner specified in Section **267(b)** to the issuer of the contract transferred in the exchange are not treated as amounts attributable to contracts entered into more than one year before such date or amounts attributable to contracts entered into more than five years before such date. (Section 1.817-5(c)(2)(iv)).

90. To obtain look-through treatment for REITs, RICs, partnerships or grantor trusts for purposes of adequate diversification rule to obtain annuity, endowment, or life insurance contract treatment, the beneficial ownership must satisfy a test and public access to such REIT, RIC, partnership or trust must be limited. As to the beneficial ownership test, investments that meet certain requirements and are held by the general account of a life insurance company or a corporation related in a manner specified in Section **267(b)** to a life insurance company or are held by the manager, or a corporation related in a manner specified in Section 267(b) to the manager, of the REIT, RIC, partnership, or trust. (Section 1.817-5(f)(3)).

91. A significant purpose to impede the assessment or collection of tax exists for purposes of disregarding a transfer of a noneconomic residual interest under Section 860E if the transferor, at the time of the transfer, either knew or should have known (had "improper knowledge") that the transferee would be unwilling or unable to pay taxes due on its share of the

taxable income of the REMIC. A transferor will be presumed not to have improper knowledge if (among other things) the transfer satisfies the asset test or the formula test. For purposes of meeting the asset test, obligations of related persons are disregarded, where a related person is any person that bears a relationship to the transferee enumerated in section **267(b) or 707(b)(1), utilizing 20%** instead of 50%, or is under common control with the transferee. (Section 1.860E-1(c)(6)(ii)).

92. If, in apportioning interest expense on the basis of assets for purposes of computing US and foreign income, the taxpayer uses the fair market value of its assets, then the taxpayer and its related persons must continue to use such method unless expressly authorized by the Commissioner to change methods, for purposes of which "related persons" means two or more persons in a relationship described in section 267(b). (Section 1.861-8T(c)(2)).

93. In apportioning research and experimentation deductions for purposes of computing US and foreign income, the residual amount is apportioned between the statutory grouping (or among the statutory groupings) within the class of gross income and the residual grouping within such class in the same proportions that the amount of sales from the product category (or categories) that resulted in such gross income within the statutory grouping (or statutory groupings) and in the residual grouping bear, respectively, to the total amount of sales from the product category (or categories). For purposes of this determination, the sales from the product category (or categories) by each party uncontrolled by the taxpayer, of particular products involving intangible property that was licensed or sold by the taxpayer to such uncontrolled party shall be taken fully into account both for determining the taxpayer's apportionment and for determining the apportionment of any other member of a controlled group of corporations to which the taxpayer belongs if the uncontrolled party can reasonably be expected to benefit directly or indirectly (through any member of the controlled group of corporations to which the taxpayer belongs) from the research expense connected with the product category (or categories) of such other member, for purposes of which "uncontrolled party" means a party that is not (among others) a person with a relationship to the taxpayer specified in Section **267(b)**. (Section 1.861-17(c)(2)(i)).

94. In classifying transfers of computer programs for purposes of subchapter N of chapter 1 of the Internal Revenue Code, sections 367, 404A, 482, 551, 679, 1059A, chapter 3, chapter 5, sections 842 and 845 (to the extent involving a foreign person), and transfers to foreign trusts not covered by section 679, a transferee of a computer program shall not be considered to have the right to distribute copies of the program to the public if it is permitted to distribute copies of the software to only either a related person (within the meaning of Section **707(b)(1)** and certain parts of **267(b), utilizing 10%** instead of 50%), or to identified persons who may be identified by either name or by legal relationship to the original transferee. (Section 1.861-18(g)(3)(i)).

95. Section 864(f)(5)(A) allows certain financial corporations, which would not be included within the affiliated group under Section 864(f)(4), to be included in the worldwide affiliated group for purposes of allocating certain expenses among the group. For purposes of Section 864(f) (as effective for taxable years beginning after December 31, 2008), the term "financial corporation" is defined as any corporation if at least 80% of its gross income is "financial services income" (within the meaning of Section 904(d)(2)(D)(ii)) which is derived

from transactions with persons who are not related (within the meaning of Section **267(b) or 707(b)(1)**) to the corporation. (Section 864(f)(5)(B)).

96. For certain purposes, if a person acquires (directly or indirectly) a trade or service receivable from a related person, any income (including any stated interest, discount or service fee) derived from the trade or service receivable shall be treated as if it were interest received on a loan to the obligor under the receivable, for purposes of which a "related person" is a person who is a related person within the meaning of Section **267(b)** and the regulations thereunder; a United States shareholder (as defined in Section 951(b)); or a person who is related (within the meaning of Section **267(b)** and the regulations thereunder) to a United States shareholder. (Section 1.864-8T(b)(2)).

97. As an anti-abuse rule, if a taxpayer recognizes loss with respect to personal property and the taxpayer (or any person described in Section **267(b)** (after application of Section 267(c)), 267(e), 318 or 482 with respect to the taxpayer) holds (or held) offsetting positions with respect to such property with a principal purpose of recognizing foreign source income and United States source loss, the loss shall be allocated and apportioned against such foreign source income. (Section 1.865-1(c)(6)(ii); see similar rule as to stock in Section 1.865-2(b)(4)(ii)).

98. Portfolio interest does not include interest that is determined with reference to receipts, sales, cash flow, income, profits, change in value of property, dividends, partnership distributions or similar payments of the debtor or a person related to the debtor within the meaning of Section **267(b) or 707(b)(1)**. (Section 871(h)(4)(B)).

99. In certain circumstances, the Service may disregard, for purposes of Section 881, the participation of one or more intermediate entities in a financing arrangement where such entities are acting as conduit entities. For this purpose, if two (or more) financing transactions involving two (or more) related persons would form part of a financing arrangement but for the absence of a financing transaction between the related persons, the district director may treat the related persons as a single intermediate entity if he determines that one of the principal purposes for the structure of the financing transactions is to prevent the characterization of such arrangement as a financing arrangement. In addition, stock in a corporation (or a similar interest in a partnership or trust) will constitute a financing transaction only if (among other things) the owner of the stock or similar interest has the right to require a person related to the issuer (or any other person who is acting pursuant to a plan or arrangement with the issuer) to acquire the stock or similar interest or make a payment with respect to the stock or similar interest. In both situations, "related" means related within the meaning of Sections **267(b) or 707(b)(1)**, or controlled within the meaning of Section 482. (Section 1.881-3(a)(2)(v)).

100. As an example of certain activities of a foreign corporation engaged in the international operation of ships or aircraft that are so closely related to the international operation of ships or aircraft that they are considered incidental to such operation, and thus deemed to be income derived from the international operation of ships or aircraft, the provision (either by subcontracting or otherwise) for the carriage of cargo preceding or following the international carriage of cargo under a through bill of lading, airway bill or similar document through a related corporation or through an unrelated person (and the rules of Section **267(b)** shall apply for

purposes of determining whether a corporation or other person is related to the foreign corporation). (Section 1.883-1(g)(1)(v)).

101. In determining whether certain corporations are sufficiently owned by foreign persons to qualify for certain exemptions for shipping and aircraft income, publicly traded corporations. For purposes of determining whether a corporation is publicly traded, if 5-percent shareholders (treating persons related within the meaning of Section 267(b) as one person) own 50% or more of the vote and value of the outstanding stock, the class of stock owned by such shareholders will not be treated as publicly traded. In addition, trades between or among related persons described in Section **267(b)** and trades conducted in order to meet the publicly traded requirements are be disregarded (Section 1.883-2(d)(3)(iii)(A) and (d)(4); see similar rules applicable in the branch profits context in Section 1.884-5(d)(4)(iii)(B) and (d)(4)(iv)).

102. The one-time exemption for Canadian corporations from the branch profits tax is reduced by the amount of any exemption that reduced the dividend equivalent amount of an associated foreign corporation with respect to the same or a similar business, for purposes of which an "associated foreign corporation" includes a foreign corporation related to the foreign corporation for purposes of Section **267(b)**. (Section 1.884-1(g)(4)(iv)(B)(2)).

103. For purposes of the rules relating to payments by related foreign interest holders to reverse hybrid entities under Treas. Reg. 1.894-1(d)(2)(ii)(B), a person will be treated as related to a reverse hybrid entity if it is related by reason of the ownership requirements of section **267(b) or 707(b)(1), utilizing "at least 80%"** instead of "more than 50%". (Section 1.894-1(d)(2)(ii)(B)(4)).

104. If a domestically controlled qualified investment entity's distribution would be treated as gain from the sale or exchange of a U.S. real property interest but for the disposition of the interest in such entity by the taxpayer during the 30-day period preceding the ex-dividend date and if the foreign person or a person related (within the meaning of Section **267(b) or 707(b)(1)**) to the foreign person acquires the interest during the 61-day period beginning with the 1st day of the 30-day period preceding the ex-dividend date, the taxpayer will still be treated as having gain from the sale or exchange of a U.S. real property interest as to such distribution. (Section 897(h)(5)(B)).

105. Any interest which is paid or accrued by a United States-owned foreign corporation during any taxable year, is paid or accrued to a United States shareholder (as defined in Section 951(b)) or a related person (within the meaning of Section **267(b)**) to such a shareholder, and is properly allocable (under regulations) to income of such foreign corporation for the taxable year from sources within the United States, shall be treated as derived from sources within the United States. (Section 904(h)(3)).

106. Financial services income for purposes of the limitations on the foreign tax credit means certain income derviced by a financial services entity. A "financial services entity" means an individual or entity that is predominantly engaged in the active conduct of a banking, insurance, financing, or similar business (active financing business) for any taxable year, i.e., if at least 80% of its gross income fits the income categories for financial services income. For purposes of that test, gross income includes all income realized by an individual or entity,

whether includible or excludible from gross income under other operative provisions of the Code, but excludes gain from the disposition of stock of a corporation that prior to the disposition of its stock is related to the transferor within the meaning of Section **267(b)**. (Section 1.904-4(e)(3)(i)).

107. Section 907(c)(2) does not apply as to "foreign oil related income" for purposes of the foreign tax credit adjustment of Section 907(b) if neither that person nor a related person has foreign oil and gas extraction income (other than directly related income) or foreign oil related income (other than directly related income) or less than 50% of that person's gross income from sources outside the United States which is related exclusively to the performance of services and from the lease or license of certain property is attributable to services performed for (or on behalf of), leases to, or licenses with, related persons. For both purposes, a person will be treated as a related person if that person would be so treated within the meaning of Section 954(d)(3) (as applied by substituting the word "corporation" for the word "controlled foreign corporation") or that person is a partnership or partner described in Section **707(b)(1)**. (Section 1.907(c)-1(g)(4)).

108. Certain portions of the calculations relevant to determining the possession tax credit under Section 936 are made without regard to transactions with related persons, where the relationship must be among a controlled group of corporations or as specified in Section **267(b) or 707(b)(1), utilizing 10%** instead of 50%. (Section 936(h)(3)(D)).

109. Certain investments in certain Caribbean Basin countries will qualify as investment in Puerto Rico so long as (among other things) the investment is in active business assets, which includes capital expenditures for the acquisition, construction, rehabilitation (including demolition associated therewith), improvement, or upgrading of qualified assets. "Qualified assets" includes rights to intangible property that is a patent, invention, formula, process, design, pattern, know-how, or similar item, or rights under a franchise agreement, provided that such rights (among other things) are not rights acquired by the qualified recipient from a person related (within the meaning of Section **267(b), using "10 percent"** instead of "50 percent" in the places where it appears) to the qualified recipient. (Section 1.936-10(c)(4)(ii)(C)(3)).

110. The income of two or more controlled foreign corporations ("CFCs") shall be aggregated and treated as the income of a single corporation if a principal purpose for separately organizing, acquiring, or maintaining such multiple corporations is to prevent income from being treated as foreign base company income or insurance income under the de minimis test. Two or more CFCs are presumed to have been organized, acquired or maintained to prevent income from being treated as foreign base company income or insurance income under the de minimis test if the corporations are related persons and the corporations satisfy other requirements, including that the corporations carry on a business, financial operation, or venture as partners directly or indirectly in a partnership that is a related person (as described in Section **267(b)(10)**) with respect to each such CFC. (Section 1.954-1(b)(4)(iii) and 4.954-1(b)(4)(iii)).

111. If a dollar election is made for an eligible qualified business unit ("electing QBU"), then the dollar shall be the functional currency of any related person (regardless of when such person became related to the electing QBU) that is an eligible qualified business unit, or

any branch of any such related person that is an eligible qualified business unit, for purposes of which the term "related person" means any person with a relationship defined in Section **267(b)** to the electing QBU (or to the United States or foreign person of which the electing QBU is a part). (Section 1.985-2(d)(3)(i)).

112. Each person that is related to the taxpayer on the last day of any taxable year for which an election to apply Treas. Reg. 1.985-3 to open taxable years is effective and that would have been eligible to elect United States dollar approximate separate transactions method of accounting ("DASTM") must also apply these rules to that year and all subsequent years. In determining whether a qualified business unit ("QBU") meets the thresholds for qualifying for the use of the small QBU DASTM allocation, a QBU shall be treated as owning all of the assets of each related QBU having its residence in the QBU's country of residence. Once the election has been made to use the small QBU DASTM allocation, each QBU of any related person that satisfies the threshold requirements shall be deemed to have made the election. For purposes of these rules, the term "related person" means any person with a relationship to the QBU (or to the United States or foreign person of which the electing QBU is a part) that is defined in Section **267(b) or 707(b)**. (Section 1.985-3(e)(2)(vi)).

113. For purposes of applying Section 988(c)(1)(E), which exempts certain forward contracts, futures contracts, options and similar financial instruments from the definition of "Section 988 transactions" (on which gains or losses are characterized in certain circumstances as ordinary income) in the case of qualified funds, interests in a partnership held by persons related to each other (within the meaning of Section **267(b) or 707(b)(1)**) are treated as held by one person. (Section 988(c)(1)(E)(vi)(I)).

114. If a debt instrument denominated in a nonfunctional currency (or the payments of which are determined with reference to a nonfunctional currency) is entered into between related persons as defined in Sections **267(b) and 707(b)**, and the instrument is disposed of or otherwise terminated prior to maturity in a transaction in which exchange gain or loss would be recognized, the District Director or the Assistant Commissioner (International) may defer such gain or loss if he determines that the debt has in effect been replaced with other debt denominated in a different currency (replacement debt) entered into with the same or another related person (regardless of whether the replacement debt is denominated in, or determined by reference to, the taxpayer's functional currency. (Proposed Section 1.988-2(b)(14)(i)).

115. For purposes of integrating certain nonfunctional currency debt instruments and certain hedges or integrating certain qualified payments and certain hedges, one requirement is that none of the parties to the hedge have relationships defined in Section **267(b) or 707(b)**. (Section 1.988-5(a)(5)(iii) and Proposed Section 1.988-5(d)(2)(i)(D)).

116. Certain executory contracts that requires payment in a nonfunctional currency and certain hedges may be integrated and, if they are so integrated, if an executory contract is between related persons as defined in Sections **267(b) and 707(b)** and if the taxpayer disposes of the hedge or terminates the executory contract prior to the accrual date, the Commissioner may redetermine the timing, source, and character of gain or loss from the hedge or the executory contract if he determines that a significant purpose for disposing of the hedge or terminating the executory contract prior to the accrual date was to affect the timing, source, or character of

income, gain, expense, or loss for Federal income tax purposes. (Section 1.988-5(b)(4)(iii)(C)). A similar rule has been proposed as to integrated qualified payments and hedges. (Proposed Section 1.988-5(d)(3)(iii)(C)(1)).

117. If a taxpayer elects the mark to market method of accounting of Treas. Reg. 1.988-5(f), each person who is related to the taxpayer within the meaning of Section **267(b) or 707(b)** (whether or not such person uses U.S. GAAP) shall be deemed to make such election. (Section 1.988-5(f)(4)).

118. For purposes of the regulations under Section 993, a "related person" means a person who is related to another person if either immediately before or after a transaction the relationship between such persons would result in a disallowance of losses under Section **267 or 707(b)** or using a modified controlled group definition. (Section 1.993-1(a)(6)).

119. For purposes of the debt modification rules of Treas. Reg. 1.1001-3, an option is unilateral (which could allow its exercise to avoid triggering a modification) only if, under the terms of an instrument or under applicable law there does not exist at the time the option is exercised, or as a result of the exercise, a right of the other party to alter or terminate the instrument or put the instrument to a person who is related (within the meaning of Section **267(b) or 707(b)(1)**) to the issuer; the exercise of the option does not require the consent or approval of the other party, a court or arbitrator or a person who is related to that party (within the meaning of Section **267(b) or 707(b)(1)**), whether or not that person is a party to the instrument; and the exercise of the option does not require consideration (other than incidental costs and expenses relating to the exercise of the option), unless, on the issue date of the instrument, the consideration is a de minimis amount, a specified amount, or an amount that is based on a formula that uses objective financial information (as defined in §1.446-3(c)(4)(ii)). (Section 1.1001-3(c)(3)).

120. The nonrecognition rule provided by Section 1031 is not available in certain circumstances if a taxpayer exchanges property with a person bearing a relationship to the taxpayer described in Section **267(b) or 707(b)(1)**. (Section 1031(f)).

121. For purposes of the deferred exchange rules under Treas. Reg. 1.1031(k)-1, a "disqualified person" includes any person that bears a relationship to the taxpayer described in either Section 267(b) or 707(b), utilizing 10% instead of 50%, or any person that bears a relationship to certain agents of the taxpayer described in either Section **267(b) or 707(b), utilizing 10%** instead of 50%. (Section 1.1031(k)-1(k)(3) and (4)).

122. The nonrecognition rule provided by Section 1033 as to involuntary conversion is not available to (among others) partnerships in which one or more C corporations own, directly or indirectly, more than 50% of the capital interest or profits interest in such partnership at the time of the involuntary conversion if the replacement property or stock is acquired from a person that bears a relationship to the acquiring person described in Section **267(b) or 707(b)(1)**. (Section 1033(i)).

123. Certain information requirements are imposed on 10% owners of an entity that transfer interests in such entity if, in connection with the transfer, such owner (or a person who is

related within the meaning of Section **267(b) or 707(b)(1)** to such owner) enters into an employment contract, covenant not to compete, royalty or lease agreement or other agreement with the transferee. (Section 1060(e)).

124. The partial exclusion for gains from certain small business stock is not applicable to stock acquired by a taxpayer if, at any time during the 4-year period beginning on the date 2 years before the issuance of such stock, the issuing corporation purchased (directly or indirectly) any of its stock from the taxpayer or a person related (within the meaning of Section **267(b) or 707(b)**) to the taxpayer. (Section 1202(c)(3)(A)).

125. The partial exclusion for gains from certain small business stock is not applicable if the taxpayer has an offsetting short position with respect to such stock, with one exception. The determination of whether there is an offending offsetting short position and whether the exception applies is made treating the taxpayer and any person related within the meaning of Section **267(b) or 707(b)** to the taxpayer as one person. (Section 1202(j)).

126. If an obligation is issued at a discount by a corporation and if (among other things) at the time of original issue there was no intention to call the obligation before maturity, the gain realized upon the sale or exchange of the obligation (if held more than 1 year) is treated as long-term capital gain. Examples of evidence that there was no understanding at the time of original issue to redeem the obligation before maturity include the original purchaser and the issuer are not related within the meaning of Section **267(b)** and have not engaged in transactions with each other (other than concerning the obligation) and the original purchaser is not related within the meaning of Section **267(b)** to any of the officers or directors of the issuer, and he has not engaged in transactions with such officers or directors (other than concerning the obligation). (Section 1.1232-3(b)(4)(ii)(b)).

127. The provision transforming certain transfers of patents into long-term capital gains is inapplicable to transfers, directly or indirectly, between persons specified within section **267(b)** (with certain modifications) **or 707(b), utilizing "25% or more"** instead of "more than 50%". (Section 1235(d)).

128. Gain for the sale of depreciable property between a person and (among others) all partnerships more than 50% of the capital interest or profits interest in which is owned (directly or indirectly) by or for such person or any entity which is a related person to such person under paragraph (3) , **(10)**, (11) , or (12) of section **267(b)** is re-characterized as ordinary income. (Section 1239(c).)

129. Section 1245 costs are properly chargeable to property if (among other times) the property is an operating or a nonoperating mineral interest held by a taxpayer if a party related to the taxpayer (within the meaning of Section **267(b) or 707(b)**) held an operating mineral interest in the same tract or parcel of land that terminated (in whole or in part) without being disposed of (e.g., a working interest which terminated after a specified period of time or a given amount of production), but only if there exists between the related parties an arrangement or plan to avoid recapture under section 1254. In such a case, the taxpayer's section 1254 costs with respect to the property include those of the related party. (Section 1.1254-1(b)(2)(iv)(A)(4)).

130. Section 1259 requires recognition of gain on any constructive sale or appreciated financial position. In determining whether a taxpayer has an appreciated financial position, the taxpayer may ignore straight debt that is not convertible (directly or indirectly) into the stock of the issuer or any related person. In determining whether a constructive sale occurs, the transactions of the taxpayer and related persons are relevant, which is then taken into account as to other appreciated financial positions. For purposes of these determinations as to related persons, the transaction must be entered into with a view toward avoiding the purpose of Section 1259 and the persons must bear a relationship described in Section **267(b) or 707(b)**. (Section 1259(c)(4) as implemented by Section 1259(b)(2)(A)(iii), 1259(c)(1) and 1259(e)(1)).

131. For purposes of Section 1272, an option is ignored if it is an option to convert a debt instrument into the stock of the issuer, into the stock or debt of a related party (within the meaning of Section **267(b) or 707(b)(1)**), or into cash or other property in an amount equal to the approximate value of such stock or debt. (Section 1.1272-1(e)).

132. The issue price of a debt instrument includes any amount paid for an option to convert the instrument into stock (or another debt instrument) of either the issuer or a related party (within the meaning of Section **267(b) or 707(b)(1)**) or into cash or other property in an amount equal to the approximate value of such stock (or debt instrument). (Section 1.1273-2(j)).

133. The discount rate for any debt instrument, given in consideration for the sale or exchange of any property (where, pursuant to a plan, the transferor or any related person leases a portion of such property after such sale or exchange), as used under Section 1274(b)(2)(B) or 483(b) shall be 110% of the AFR, compounded semiannually, and Section 1274A does not apply to any such debt instrument. (Section 1274(e)). For purposes of these rules, a "related person" means a person related to the transferor within the meaning of Section **267(b) or 707(b)(1)**. (Section 1.1274-4(a)(2)(i)).

134. A debt instrument does not provide for contingent payments for purposes of the contingent payment debt instrument rules merely because it provides for an option to convert the debt instrument into the stock of the issuer, into the stock or debt of a related party (within the meaning of Section **267(b) or 707(b)(1)**), or into cash or other property in an amount equal to the approximate value of such stock or debt. (Section 1.1275-4(a)(4)).

135. For purposes of determining whether a debt instrument is a variable rate debt instrument, an objective rate (which is required under certain circumstances) does not include a rate based on information that is within the control of the issuer (or a related party within the meaning of Section **267(b) or 707(b)(1)**) or that is unique to the circumstances of the issuer (or a related party within the meaning of Section **267(b) or 707(b)(1)**). (Section 1.1275-5(c)(1)(ii)).

136. With certain exceptions, a qualifying debt instrument and a Section 1.1275-6 hedge are an integrated transaction if (among other things) none of the parties to the Section 1.1275-6 hedge are related within the meaning of Section **267(b) or 707(b)(1)**, or, if the parties are related, the party providing the hedge uses, for federal income tax purposes, a mark-to-market method of accounting for the hedge and all similar or related transactions. (Section 1.1275-6(c)(1)(ii)).

137. The circumstances under which the Commissioner may require integration of a qualifying debt instrument and a Section 1.1275-6 hedge include (among others) a taxpayer issues or acquires a qualifying debt instrument and a related party (within the meaning of Section **267(b) or 707(b)(1)**) enters into the §1.1275-6 hedge and a taxpayer issues or acquires a qualifying debt instrument and enters into the §1.1275-6 hedge with a related party (within the meaning of Section **267(b) or 707(b)(1)**). (Section 1.1275-6(c)(2)).

138. With certain exceptions, the use of stock of a Section 1291 fund as security for the performance of an obligation of a direct or indirect shareholder (or of a person related within the meaning of Section **267(b)** to that shareholder), in connection with a loan, guarantee, margin account, or otherwise (a pledge of stock), is a transaction that results in a disposition of the stock of the section 1291 fund. (Section 1.1291-3(d)(1)).

139. For purposes of determining the empowerment zone employment credit, any amount paid or incurred by an employer which is excludable from the gross income of an employee under Section 127 will be treated as wages, but only to the extent paid or incurred to a person not related to the employer, where a person will be treated as related to the employer if the person and the employer are engaged in trades or businesses under common control or the person bears a relationship to the employer specified in Section **267(b) or 707(b)(1), utilizing 10%** instead of 50%. (Section 1397(a)(2)).

140. The exclusion for certain capital gains from the sale or exchange of certain District of Columbia Enterprise Zone assets does not apply to capital gains attributable, directly or indirectly, in whole or in part, to a transaction with a person related to the disposing person if such persons are described in Section **267(b) or 707(b)(1)**. (Section 1400B(e)(5)).

141. The credit allowable for first-time homebuyers in the District of Columbia is not available if the home is acquired from a person whose relationship to the acquiring person would result in the disallowance of losses under Section **267 or 707(b)**. (Section 1400C(e)(2)(A)(i)).

142. For withholding under Section 1441, a withholding agent may rely on documentation furnished by a customer for an account held at another branch location of the same withholding agent or at a branch location of a person related (within the meaning of Section **267(b) or 707(b)**) to the withholding agent if the withholding agent and the related person are part of a universal account system that uses a customer identifier that can be used to retrieve systematically all other accounts of the customer. (Section 1.1441-1(e)(4)(ix)(A)(2)).

143. If a member of a consolidated group, M, would otherwise recognize gain on a qualified disposition of the stock of the parent of such consolidated group (P), then immediately before the qualified disposition, M is treated as purchasing the P stock from P for fair market value with cash contributed to M by P (or, if necessary, through any intermediate members). For purposes of this rule, a "qualified disposition" must (among other things) include M transferring the stock immediately to a nonmember that is not related, within the meaning of Section **267(b) or 707(b)**, to any member of the group, pursuant to a plan. (Section 1.1502-13(f)(6)(ii)(B)).

144. The amount of loss disallowed under Treas. Reg. 1.1502-20(a)(1) and the amount of basis reduction under Treas. Reg. 1.1502-20(b)(1) with respect to a share of stock shall not

exceed the sum of the extraordinary gains, the positive investment adjustments and the duplicate losses, the first two of which are not reduced or eliminated by reason of an acquisition of the share from a person related within the meaning of Section **267(b) or 707(b)(1), utilizing 10%** instead of 50%, even if the share is not transferred basis property as defined in Section 7701(a)(43). For purposes of the duplicate loss calculation, stock is acquired by purchase if the transferee is not related to the transferor within the meaning of Sections **267(b) and 707(b)(1), utilizing 10%** instead of 50%. (Section 1.1502-20(c)(2)(iv) and 1.1502-20(c)(2)(vi); see also Section 1.1502-35(d)(4)(ii)(A)).

145. For purposes of determining whether an item should be included in a consolidated return, if, on the day of a subsidiary corporation's change in status as a member, a transaction occurs that is properly allocable to the portion of the subsidiary corporation's day after the event resulting in the change, subsidiary corporation and all persons related to the subsidiary corporation under Section **267(b)** immediately after the event must treat the transaction for all Federal income tax purposes as occurring at the beginning of the following day. (Section 1.1502-76(b)(1)(ii)(B)).

146. For purposes of Treas. Reg. 1.1504-4, Persons are related if they are related within the meaning of section **267(b)** (with certain modifications) **or 707(b)(1), utilizing 10%** instead of 50%. (Section 1.1504-4(c)(3)).

147. If an interest in a corporation or partnership (an "entity") is transferred to or for the benefit of a member of the transferor's family (where the transferor and members of the transferor's family control the entity immediately before the transfer), any applicable restriction is disregarded in valuing the transferred interest. An applicable restriction does not include a commercially reasonable restriction on liquidation imposed by an unrelated person providing capital to the entity for the entity's trade or business operations whether in the form of debt or equity, for purposes of which "unrelated person" means any person whose relationship to the transferor, the transferee, or any member of the family of either is not described in Section **267(b)**. (Section 25.2704-2(b)).

148. In determining the applicability of the 50% tax on "greenmail," public tender offers made or threatened by persons related to certain shareholders or any person acting in concert with such shareholders are taken into account, where the relationship would result in the disallowance of losses under Section **267 or 707(b)**. (Section 5881(b)(2)(C)).

149. For purposes of determining whether an advisor that has imposed conditions of confidentiality has caused a transaction to be a reportable transaction and determining whether the minimum fee threshold has been met, persons who bear a relationship to each other as described in Section **267(b) or 707(b)** will be treated as the same person. (Section 1.6011-4(b)(3)(v)).

150. A transaction is a reportable transaction as one with contractual protection if it is a transaction for which the taxpayer or a related party (as described in Section **267(b) or 707(b)**) has the right to a full or partial refund of fees if all or part of the intended tax consequences from the transaction are not sustained. (Section 1.6011-4(b)(4)(i)).

151. The book-tax difference type of reportable transaction only applies to taxpayers that are reporting companies under the Securities Exchange Act of 1934 (15 U.S.C. 78a) and related business entities (as described in Section **267(b) or 707(b)**); or business entities that have $250 million or more in gross assets for book purposes at the end of any financial accounting period that ends with or within the entity's taxable year in which the transaction occurs, for purposes of which the assets of all related business entities (as defined in Section **267(b) or 707(b)**) must be aggregated. (Section 1.6011-4(b)(6)(ii)(A)).

152. The reporting requirements imposed on domestic corporations that are 25% foreign owned include information requirements regarding persons who are related (within the meaning of Section **267(b) or 707(b)(1)**) to the reporting corporation or to a 25% foreign shareholder of the reporting corporation. (Section 6038A(b)).

153. A U.S. person that transfers cash to a foreign corporation in certain types of transfers must report the transfer if (among other things) the amount of cash transferred by such person or any related person (determined under Section **267(b)**(1) through (3) and **(10)** through (12)) to such foreign corporation during the 12-month period ending on the date of the transfer exceeds $100,000. (Section 1.6038B-1(b)(3)).

154. The reporting requirements under Section 6038B are imposed on transfers of property by U.S. persons to foreign partnerships in a contribution described in Section 721 if immediately after the transfer, the U.S. person owns, directly, indirectly, or by attribution, at least a 10% interest in the partnership, as defined in section 6038(e)(3)(C) and the regulations thereunder; or the value of the property transferred, when added to the value of any other property transferred in a section 721 contribution by such person (or any related person) to such partnership during the 12-month period ending on the date of the transfer, exceeds $100,000. In complying with the reporting requirements imposed under Section 6038B, the names and address of persons related to the transferor during that tax year must be disclosed. For purposes of these rules, a person is related if they bear a relationship described in Section **707(b)(1)(B) or** certain portions of Section **267(b)**. (Section 1.6038B-2(i)(4)).

155. For purposes of determining whether the information reporting requirements of Section 6050H apply, interest received from a seller or a person related to a seller within the meaning of Section **267(b) or 707(b)(1)** on a payor of record's mortgage is not interest received on a mortgage. (Section 1.6050H-1(e)(3)(i)).

156. Reporting is specifically required under Section 6114 (among other times) if a taxpayer takes the position that a treaty exempts from tax, or reduces the rate of tax on, fixed or determinable annual or periodical income subject to withholding under Section 1441 or 1442 that a foreign person receives from a U.S. person, but only if (among other times), with respect to a treaty that contains a limitation on benefits article, the treaty exempts from tax, or reduces the rate of tax on income subject to withholding (as defined in Treas. Reg. 1.1441-2(a)) that is received by a foreign person (other than a State, including a political subdivision or local authority) that is the beneficial owner of the income and the beneficial owner is related to the person obligated to pay the income within the meaning of Sections **267(b) and 707(b)**, and the income exceeds $500,000 and a foreign person (other than an individual or a State, including a

political subdivision or local authority) meets the requirements of the limitation on benefits article of the treaty. (Section 301.6114-1(b)(4)(ii)(C)).

157. An error or delay in performing a ministerial or managerial act will be taken into account for purposes of abating underpayment interest only if no significant aspect of the error or delay is attributable to the taxpayer involved or to a person related to the taxpayer within the meaning of Section **267(b) or 707(b)(1)**. (Section 301.6404-2(a)(2)).

158. For an advisor's opinion to be used to establish a reasonable cause defense to certain penalties, among other things, the advisor must not be a material advisor that participates in the organization, management, promotion or sale of the transaction or that is related (within the meaning of Section **267(b) or 707(b)(1)**) to any person who so participates. (Section 6664(d)(3)(B)(ii)(I)).

159. The prohibition on the Secretary utilizing summons proceedings to obtain tax-related computer software source code does not apply to (among other things) any such code acquired or developed by the taxpayer or a related person primarily for internal use by the taxpayer or such person rather than for commercial distribution or any communications between the owner of such code and the taxpayer or related persons, in each case where the relationship would cause the persons to be related under Section **267 or 707(b)**. (Section 7612(b)(2)(B) and (C)).

160. For purposes of a transition rule under Treas. Reg. 301.7701-2, a rule eliminating grandfathered status on a Section 708(b)(1)(B) termination will not apply if the sale or exchange of interests in the entity is to a related person (within the meaning of Sections **267(b) and 707(b)**) and occurs no later than twelve months after the date of the formation of the entity. (Section 301.7701-2(d)(3)(ii)).

161. For purposes of the block transfer type of private transfer under the publicly traded partnership rule, transfers by related persons are considered. For purposes of the transfers pursuant to certain redemption or repurchase agreement type of private transfer, agreements contemplating transfers to persons related to partners are considered. For purposes of the closed end redemption plan type of private transfer, no partner or person related to any partner may provide a contemporaneous opportunity to acquire interests in similar or related partnerships which represent substantially identical investments. For purposes of the matching service safe harbor under the publicly traded partnership rules, the timing of closing is important and, for this purpose, closing occurs no later than the earlier of passage of title, payment of the purchase price or the date, if any, that the operator of the matching service (or any person related to the operator) loans, advances, or otherwise arranges for funds to be available to the seller in anticipation of the payment of the purchase price. For purposes of applying the publicly traded partnership rules, the total interests in partnership capital or profits are determined by reference to all outstanding interests in the partnership except (among other times) where the general partners and any person related to the general partners own, in the aggregate, more than 10% of the outstanding interests in partnership capital or profits at any one time during the taxable year of the partnership. In each case, a "related person" is determined under the meaning of Section **267(b) or 707(b)(1)**. (Sections 1.7704-1(e)(2), -1(e)(3), -1(e)(4)(ii), -1(g)(3) and -1(k)(1)(ii)(A)).

162. For purposes of the rules relating to Section 7874, the term "expatriated entity" includes any U.S. person who is related (within the meaning of Section **267(b) or 707(b)(1)**) to a domestic corporation or partnership with respect to which a foreign corporation is a surrogate foreign corporation. (Section 7874(a)(2)(A)(ii)).

163. For purposes of the rules relating to Section 7874, the term "inversion gain" includes income or gain by reason of certain transfers or licenses to a foreign person which is under the same common control as the expatriated entity or is related (within the meaning of Section **267(b) or 707(b)(1)**) to such entity. (Section 7874(d)(2) and (3)).

APPENDIX III

PARTNERSHIP PERCENTAGE INTEREST THRESHOLDS

Percentage Threshold	Source
Any capital or profits interest	267(e)(1)(B)(i) and (C) 1.267(a)-2T(c), Answer 2 25.2701-2(b)(5)(iii)
Less than 1% of profits	6223(b)(1)
1% or more of capital or profits	1.61-21(f)(5)(iv)
More than 1% of capital or profits	1.416-1, T-16
2% or less of capital of profits	1.7704-1(j)
More than 2% of capital or profits	1.7704-1(e)(2)
Less than 5% of capital and profits	267(e)(5)(A)(i) and (B)
5% or more of capital and profits	1.367(a)-3(c)(5)(viii)(B)
5% or more of capital or profits	1.61-21(g)(8)(i)(C) 1.414(c)-3(d)(2)(iii) 1.414(c)-4(b)(2) 613A(d)(3)(B) 706(b)(3) 1563(e)(2)
5% or more of profits	6223(b)(2) 6231(a)(11)
More than 5% of capital or profits	120(c)(3) 127(b)(3) 1.414(q)-1T, Q&A-8 1.416-1, T-17
Less than 10% interest in capital and profits	163(j)(4)(B)(i) 1.706-1(b)(6)(iii) 1.861-9T(e)(4)(i) and (ii) 1.904-5(h)(4) 1.1374-4(i)(5)(i)
10% or less interest in capital or profits	1.7704-1(f)(3) and (g)(2)(vii)

10% or more of capital or profits	1.643(h)-1(e)* 1.679-3(c)* 4975(e)(2)(I)
10% or greater interest	1.861-9T(e)(2) and (3)
10% or more interest in capital and profits	1.904-5(h)(4)
10% or more interest in capital or profits or deductions or losses	1.6038-3(b)(3)
10% or more interest in profits and losses	465(c)(7)(D)(ii)(II)
More than 10% of capital or profits	42(d)(2)(D)(iii)(I) 42(d)(2)(D)(iii)(II) 1.168-4(d)(6) 401(c)(3)(D) 465(b)(3)(C) 1.706-1(b)(6)(iii) 1.861-18(g)(3)(i) 936(h)(3)(D) 1.1031(k)-1(k)(3) and (4) 1397(a)(2) 1.1502-20(c)(2) and -35(d)(4)(ii)(A) 1.1504-4(c)(3) 1.7704-1(k)(ii)(A)
More than 10% of profits	4951(e)(4)(C)(ii)
Less than 20% interest in capital and profits	1.706-1(b)(6)(iii)
20% or less of profits	1563(c)(2)(A) and (3)(A)
20% or more of profits or capital	1.83-7(a)(1)* 197(f)(9)(C)* 1.305-5(b)(3)(ii)(A)* 1.409A-1(f)(3)* 1.860E-1(c)(6)(ii)* 4943(c)(3)(A)
20% or more of capital	20.2056A-2(d)(1)(ii)(B) 6166(b)(1)(B)(i)
20% or more of the partner's highest interest in any item of loss or deduction	1.752-4(b)(2)(iv)(A)(2) and (B)(1)
More than 20% of profits	4943(f)(4)(B)(iii)(II)

25% or more of capital and profits	1.367(a)-3(c)(5)(viii)(A)(2)
25% or more of capital or profits	512(b)(19)(J)* 954(c)(4)(B) 1235(d)*
30% or more of capital	2057(e)(1)(B)(ii) and (3)(A)(ii)
35% or less of profits	501(q)(1)(E)(ii)
More than 35% of profits	4951(e)(4)(G) 4958 (f)(3)(A)(ii)
50% or more of capital and profits	708(b)(1)(B) 1.7704-1(e)(1)(ix)
50% or more of capital or profits	1.42-6(b)(2)(iv)(E)* 45D(f)(2)(B)* 101(j)(3)(B)(ii)(I)* 108(e)(4)* 121(d)(8)(B)* 144(a), 144(c)* 147(a)(2)(A)* 163(e)(3)(C)* 163(j)(4)(A)* 163(l)(6)* 165(l)(2)* 167(e)(5)(B)* 167(g)(5)(C)* 1.167(l)-1(e)(4)(ii)(b)(1)* 168(k)(2)(E)(iv)(I)* 1.168(k)-1T(b)(3)(iv)* 1.168(h)-1* 170(a)(3)* 1.170A-13(c)(5)(iv)(E)* 1.170A-14(g)(4)(ii)(A)(2)* 1.170A-14(h)(3)(i)* 1.171-1(e)(1)(iii)(C)* 179(d)(2)* 179A(b)(2)(B)* 1.197-2(e)(3)* 213(d)(11)(B)* 221(d)(1)* 1.246-5(c)(6)* 1.263(a)-4 and -5* 1.263A-3(a)(3) and -3(a)(4)(iii)* 1.263A-3(c)(4)(vi)(A)(2)*

1.263A-8(a)(4)(i)*
1.267(f)-1(c)(1)(iii)*
1.269B-1(b)(2)*
274(e)(2)(B)(ii)*
1.274-4(f)(5)(i)(b)*
280F(d)(6)(D)(ii)*
304(b)(5)(A)*
1.305-5(b)(2)*
1.338-8(j)(1) and (5)*
351(g)(3)(B)*
355(d)(7)(A)*
355(g)(2)(B)(ii)*
1.367(d)-1(h)(1)*
1.382-4(d)(4)(ii)(A)(2)*
409(n)(1)(A)(ii)*
1.409A-1(f)(3)*
1.414(c)-3(b)(iii) and (c)(iii)
1.446-3(c)(4)(i)*
453(g)(3)*
1.460-1(b)(4)*
1.467-1(h)(11)*
1.468B-1(d)(2)*
1.468B-9(d)(2)(ii)*
469(g)(1)(B)*
1.469-4T(j)(3)(iii)(C)*
475(c)(4)(B)(iii)*
1.475(b)-1(b)(i)*
1.475(b)-1(e)(1)(ii)(B)
453(g)(3)*
1.460-1(b)(4)*
1.461-2(c)(1)(iii)(E)*
Prop. Reg. 1.465-20(a)(2)*
1.467-1(h)(11)*
468(d)(3)*
1.468B-1(d)(2)*
1.468B-9(d)(2)(ii)*
469(g)(1)(B)*
1.469-4T(j)(3)(iii)(C)*
475(c)(4)(B)(iii)*
1.475(b)-1(b)(i)*
514(c)(9)(B)(iii)*
1.585-5(b)(2)*
613A(c)(8)(D)(ii)*
631(c)*
643(i)(2)(B)(i)*
664(g)(5)*

685(c)(2)(A)*
1.704-1(b)(2)(ii)(b)*
1.704-1T(b)(1)(ii)(b)(2)*
1.707-7(j)(8)*
755(c)*
1.817-5(c)(2)(iv)*
1.817-5(f)(3)*
1.861-8T(c)(2)*
1.861-17(c)(2)(i)*
864(f)(5)(B)*
1.864-8T(b)(2)*
1.865-2(b)(4)(ii)*
871(h)(4)(B)*
1.881-3(a)(2)(v)*
1.883-1(g)(1)(v)*
1.883-2(d)(3)(iii)(A) and (d)(4)*
1.884-1(g)(4)(iv)(B)(2)*
1.884-5(d)(4)(iii)(B) and (d)(4)(iv)*
897(h)(5)(B)*
904(h)(3)*
1.904-4(e)(3)(i)*
1.907(c)-1(g)(4)*
1.954-1(b)(4)(iii)*
1.985-2(d)(3)(i)*
1.985-3(e)(2)(vi)*
988(c)(1)(E)(vi)(I)*
1.988-2(b)(14)(i)*
1.988-5(a)(5)(iii) and -5(d)(2)(i)(D)*
1.988-5(b)(4)(iii)(C) and -5(d)(3)(iii)(C)(1)*
1.988-5(f)(4)*
1.993-1(a)(6)*
1.1001-3(c)(3)*
1031(f)*
1033(i)*
1060(e)*
1202(c)(3)(A)*
1202(j)*
1.1232-3(b)(4)(ii)(b)*
1239(c)*
1.1254-1(b)(2)(iv)(A)(4)*
1259(c)(4)*
1.1272-1(e)*
1.1273-2(j)*
1.1274-4(a)(2)(i)*
1.1275-4(a)(4)*
1.1275-5(c)(1)(ii)*

	1.1275-6(c)(1)(ii)* 1.1275-6(c)(2)* 1.1291-3(d)(1)* 1400B(e)(5)* 1400C(e)(2)(A)(i)* 1.1441-1(e)(4)(ix)(A)(2)* 1.1502-13(f)(6)(ii)(B)* 1.1502-76(b)(1)(ii)(B)* 25.2701-2(b)(5)(iii) 25.2704-2(b)* 4975(e)(2)(E)(ii) and (G) 5881(b)(2)(C)* 1.6011-4(b)(3)(v)* 1.6011-4(b)(4)(i)* 1.6011-4(b)(6)(ii)(A)* 6038A(b)* 1.6038B-1(b)(3)* 1.6038B-2(i)(4)* 1.6050H-1(e)(3)(i)* 301.6114-1(b)(4)(ii)(C)* 301.6404-2(a)(2)* 6664(d)(3)(B)(ii)(I)* 7612(b)(2)(B) and (C)* 301.7701-2(d)(3)(ii)* 1.7704-1* 7874(a)(2)(A)(ii) and (d)(2) and (3)*
50% or more of capital	2057(e)(1)(B)(i)(I) and (3)(A)(ii)
50% or more of capital or profit or loss	Schedule M-3 (Form 1065), Box D and Form 1065 Schedule M-3 (Draft Instructions), 2006, p. 2
50% or more of capital or income or loss	Form 1065 Schedule M-3 (Draft Instructions), 2006, p.2
More than 50% of capital <u>and</u> profits	1.444-2T(e)(2)(ii) 706(b)(4)(A)(i) 1.904-5(h)(4) 1.1017-(g)(2)(ii)(B) 1.7519-1T(b)(5)(iv)(D)(1)(iii) 1.7519-1T(b)(5)(iv)(D)(2)(ii)

More than 50% of capital or profits	1.52-1(c)(2)(iii) and (3)(iii) 267(a)(10) 1.401-12(l)(3)(i)(b) 1.414(c)-2(b)(2)(i)(C) 707(b)(1)(A) and (B) 1.737-1(c)(1) 1.864-2(c)(2)(i) 954(d)(3) 1033(i)(2)(b) 1239(C)(1)(B) 53.4958-4(a)(2)(ii)(B)(1)(ii)
More than 50% of capital or profits or deductions or losses	1.6038-3(b)(2)
More than 50% of profits	301.6231(a)(7)-1(e)(4) and (f)(2)(iv)
70% or more of capital	2057(e)(1)(B)(i)(II) and (3)(A)(ii)
80% or more of capital and profits	163(j)(6)(D)(ii) 775(b)(3)
80% or more of capital or profits	1.52-1(d)(2)(iii) 1.382-9(d)(5)(ii)(A)* 1.704-1(b)(2)(ii)(h)* 1.752-4(b)(1)* 1.894-1(d)(2)(ii)(B)(4)* 1.864-16(d) 1.7874-1T(c)(1)
90% or more of capital	2057(e)(1)(B)(i)(III) and (3)(A)(ii)
In accordance with partner's capital interest	704(e)(1) 743(b)(2) 1.761-2(b)(2)(b)(ii)(b) 1.856-3(g)
In accordance with partner's general profits interest	1.46-3(f)(2)
In accordance with partner's interest in profits	1.752-3(a)(3)
In accordance with partner's interest in capital or income	613A(c)(7)(D)
In accordance with capital or profits, whichever is greater	25.2701-6(a)(3)

Taking into consideration the percentage of capital and profits interests	301.6231(a)(3)-1(c)(4)(iii)
Taking into consideration the amount of the partner's profits interest	301.6231(a)(7)-1(q)(2)(iii)
In connection with the maximum percentage interest deemed owned in capital or profit or loss	Form 1065 Schedule M-3 (Draft Instructions), 2006, pgs. 3, 8
In accordance with the largest profits interest	301.6231(a)(7)-1(m)(2)

*** Contains derivative references (incorporating PIPP and/or PIPC) under 267(b) and/or 707(b)**