***5 T.C. 1371 (1945)***

A family partnership will not be recognized for federal income tax purposes if there is no material change in the economic status or management of the business, and the purported partners do not exercise real control or contribute significantly to the enterprise.

**Summary**

P.A. Keenan, Sr. and his wife, Mattie W. Keenan, sought to recognize their two minor sons as partners in their auto parts business for tax purposes. Prior to 1941, the business operated as a partnership between the parents. In January 1941, they attempted to gift portions of their partnership interests to their sons. The Tax Court held that the sons were not bona fide partners because the father retained complete control of the business, the sons' contributions were minimal, and their withdrawals were negligible. Thus, the income was taxable to the parents, not the purported family partnership.

**Facts**

The Keenan Auto Parts Co. was initially operated as a partnership between P.A. Keenan, Sr. and his wife, Mattie W. Keenan. P.A. Keenan, Sr. was the dominant figure, managing all aspects of the business. In late 1940, the Keenans discussed bringing their two sons into the business, planning to give each son a one-quarter interest. In January 1941, the firm's books were adjusted to reflect a four-way partnership with equal capital accounts for each family member. No formal partnership agreement was executed. The sons were in college and contributed minimal services during the year. P.A. Keenan, Sr. continued to manage the business and drew funds at will for personal and family expenses. Trust agreements were created later in 1941, conveying portions of the parents' interests to themselves as trustees for the sons.

**Procedural History**

The Keenan Auto Parts Co. filed a partnership return, allocating income equally among the four family members. The Keenans filed individual income tax returns reflecting this allocation. The Commissioner of Internal Revenue challenged the validity of the family partnership, asserting that the income should be taxed to the parents. The Tax Court consolidated the cases and heard the matter de novo.

**Issue(s)**

Whether the Keenan's sons were bona fide partners in the Keenan Auto Parts Co. during 1941 for federal income tax purposes, thereby allowing the family to split the business income among themselves.

**Holding**

 

No, because there was no significant change in the management, control, or economic status of the business as a result of including the sons as purported partners. The parents retained control and the sons' contributions were minimal.

## Court's Reasoning

The Tax Court emphasized that the critical inquiries in family partnership cases are: (1) the effect of the new arrangement on the economic position of the original owners, and (2) whether there was a real change in the management of the business. The court found that P.A. Keenan, Sr. maintained complete control, and the sons' contributions were insignificant. The court noted that the father's withdrawals from the partnership were not treated as distributions of partnership income, demonstrating that the sons' interests were not truly respected. The court cited *Burnet v. Leininger* as controlling, stating that formal bookkeeping entries alone were insufficient to establish a valid partnership where the father continued to manage and control the partnership property. The court concluded that the arrangements made by the Keenans had "absolutely no effect on the conduct of the business or on their own economic status therein." The court also emphasized that the earnings of the business were primarily due to the activities and acumen of Keenan, Sr., further supporting the determination that the sons had no real proprietary interest.

## Practical Implications

This case illustrates the scrutiny given to family partnerships, particularly when formed to reduce tax liability. It underscores the importance of demonstrating a real transfer of control and a significant contribution from all purported partners. The decision informs how similar cases should be analyzed by emphasizing that mere bookkeeping entries are insufficient to establish a partnership for tax purposes. Attorneys must advise clients that simply gifting partnership interests to family members is not enough; there must be a demonstrable shift in management, control, and economic benefit. Later cases have cited Keenan to reinforce the principle that family partnerships are valid only when each partner genuinely contributes to the business and exercises control proportionate to their stated interest.

 