14 T.C. 134 (1950)

Whether a partnership exists for federal tax purposes depends on whether the parties truly intended to join together in the present conduct of the enterprise, considering all facts, including the agreement, conduct, statements, relationships, contributions, control of income, and business purpose.

Summary

The Tax Court addressed whether a contract between Rosenberg and Selber created a partnership for federal tax purposes, or merely an employer-employee relationship. Rosenberg argued that his agreement with Selber, which stipulated a share of profits, constituted a partnership under the tests outlined in Commissioner v. Culbertson. The court found that no genuine intent to form a partnership existed, pointing to the contract's language designating Rosenberg as an employee, the limited scope of his responsibilities, and Selber's unrestricted control over the business's finances. Consequently, the court held that the compensation Rosenberg received was taxable as ordinary income, not as capital gains from a partnership.

Facts

Rosenberg entered into a contract with Selber Bros. Inc. to manage its retail shoe department. The contract was titled an "employment agreement." Rosenberg invested $1,500 at the beginning of his employment. The agreement provided Rosenberg with 50% of the net profits of the shoe department, termed as a "bonus." The agreement stipulated that Selber had unrestricted use of funds in the "Bonus Account." Rosenberg had no right to assign or transfer any monies credited to the Bonus Account. Selber dissolved Selber Bros. Inc. in 1943 and adopted a partnership method of doing business with his brothers, without including Rosenberg.

Procedural History

The Commissioner determined that $13,500 of the $15,000 Rosenberg received upon termination of his employment was taxable as ordinary income. The Commissioner initially included $2,150 in Rosenberg's 1943 income, which was properly includible in his 1942 income. Rosenberg petitioned the Tax Court, arguing that a partnership existed and the compensation should be treated as capital gains. The Tax Court reviewed the Commissioner's determination.

Issue(s)

Whether the agreement between Rosenberg and Selber created a partnership for federal tax purposes, entitling Rosenberg to capital gains treatment on the compensation received upon termination.

Holding

No, because considering all the facts, the parties did not genuinely intend to form a partnership; therefore, the compensation Rosenberg received is taxable as ordinary income.

Court's Reasoning

The court applied the test from *Commissioner v. Culbertson*, which examines the parties' intent to join together in the present conduct of the enterprise. The court emphasized that the contract was explicitly an employment agreement, not a partnership agreement. Rosenberg's responsibilities were limited and subject to Selber's control. Selber had unrestricted access to the bonus account, indicating Rosenberg lacked a proprietary interest. Louis Selber testified that he intended the agreement to be an employment agreement and that the provisions were carried out accordingly. The court also noted that Rosenberg was not included when Selber Bros. Inc. dissolved and the Selber brothers formed a partnership, further suggesting he was never considered a partner. The court also cited jurisprudence stating that a corporation has no implied power to become a partner with an individual. Based on these factors, the court concluded that the 50% share of net profits accrued to Rosenberg as compensation for services, not as a result of a vested interest in a partnership.

Practical Implications

This case clarifies the importance of examining the totality of circumstances to determine the existence of a partnership for federal tax purposes. The mere sharing of profits is not sufficient; the intent to form a partnership, evidenced by factors like control, capital contribution, and liability for losses, must be present. Attorneys should carefully draft agreements to clearly define the relationship between parties and ensure that the agreement reflects the actual intent of the parties. Subsequent conduct of the parties will be critical in demonstrating whether or not a partnership exists, regardless of the stated intent. Later cases have relied on *Rosenberg* to distinguish between partnerships and employer-employee relationships where profit-sharing is involved, emphasizing the need for genuine mutual control and risk-sharing for a partnership to exist.

