Peters v. Commissioner, 89 T. C. 423 (1987)

Limited partners' personal guarantees do not place them 'at risk' for amounts beyond their cash contributions when they have a right of subrogation against the partnership.

Summary

Touraine Co. , a limited partnership, entered into an equipment sale-leaseback transaction on December 31, 1978. The IRS challenged the partnership's tax year start date and the limited partners' at-risk status. The Tax Court held that Touraine's tax year began on December 29, 1978, when it acquired new partners and assets. Additionally, the court ruled that the limited partners were not at risk for amounts beyond their cash contributions because their personal guarantees were subject to a right of subrogation against the partnership. This decision clarified the application of the at-risk rules under Section 465, affecting how limited partners' liabilities are assessed in tax-motivated transactions.

Facts

Touraine Co. was initially formed on January 4, 1978, but had no assets, liabilities, or business until December 29, 1978, when it acquired new partners and significant assets. On December 31, 1978, Touraine entered into an equipment sale-leaseback transaction with Datasaab Systems, Inc. The limited partners made cash contributions and executed personal guarantees to Manufacturers Hanover Trust Co. for portions of the partnership's debt. These guarantees were structured to cover expected tax losses minus capital contributions and were legally enforceable, but limited partners retained a right of subrogation against the partnership.

Procedural History

The IRS issued deficiency notices to the petitioners, challenging the start date of Touraine's tax year and the at-risk status of the limited partners. The Tax Court consolidated the cases and heard arguments on the issues, ultimately ruling on the start date of the tax year and the at-risk status based on the personal guarantees.

Issue(s)

1. Whether Touraine's first tax year commenced on December 29, 1978, when it acquired new partners and assets.
2. Whether the limited partners were at risk for amounts beyond their cash contributions due to their personal guarantees.

Holding

1. Yes, because Touraine's partners did not have a good-faith intent to presently conduct an enterprise with a business purpose until December 29, 1978.

© 2025 SCOTUSreports.com. All rights reserved.

2. No, because the limited partners were not at risk beyond their cash contributions due to their right of subrogation against the partnership under the personal guarantees.

Court’s Reasoning

The court applied the principles from *Torres v. Commissioner* and *Sparks v. Commissioner*, determining that a partnership exists for tax purposes when the parties intend to join together in the present conduct of an enterprise. Touraine’s tax year began on December 29, 1978, when it acquired new partners and assets, reflecting this intent. Regarding the at-risk issue, the court followed *Brand v. Commissioner*, holding that the limited partners’ personal guarantees did not place them at risk beyond their cash contributions due to their right of subrogation against Touraine. The court distinguished *Abramson v. Commissioner*, noting that in *Peters*, the guarantees did not extend to the entire debt and were not primary obligations. The court emphasized that the at-risk rules aim to limit deductions to amounts for which the taxpayer is truly at risk of economic loss.

Practical Implications

This decision impacts how limited partners’ at-risk status is determined in tax-motivated transactions, particularly those involving personal guarantees. Practitioners must ensure that guarantees do not provide a right of subrogation to qualify as at-risk amounts. This ruling may lead to increased scrutiny of partnership agreements and financing structures to ensure compliance with Section 465. Businesses engaging in similar transactions should carefully structure their financing to avoid unintended tax consequences. Subsequent cases like *Brand v. Commissioner* and *Abramson v. Commissioner* continue to be distinguished based on the specifics of the guarantees and the presence of subrogation rights.

© 2025 SCOTUSreports.com. All rights reserved.