Renkemeyer, Campbell & Weaver, LLP v. Commissioner, 136 T. C. 137 (2011)

In Renkemeyer, Campbell & Weaver, LLP v. Commissioner, the U. S. Tax Court ruled that the special allocation of partnership income to a corporate partner was improper and affirmed the IRS's reallocation according to partners' profits and loss interests. Additionally, the court held that the income derived from legal services by attorney partners was subject to self-employment tax, rejecting the argument that partners in an LLP should be treated as limited partners for tax purposes.

Parties

Renkemeyer, Campbell & Weaver, LLP, and Renkemeyer, Campbell, Gose & Weaver LLP, with Troy Renkemeyer as the Tax Matters Partner, were the petitioners. The Commissioner of Internal Revenue was the respondent.

Facts

Renkemeyer, Campbell & Weaver, LLP, a Kansas limited liability partnership (LLP), engaged in the practice of law. For the tax year ended April 30, 2004, the partnership had four partners: three attorneys (Troy Renkemeyer, Todd Campbell, Tracy Weaver) and RCGW Investment Management, Inc. (RCGW), an S corporation owned by an ESOP. The three attorneys performed legal services, generating 99% of the firm's income, while RCGW's contribution was minimal. The partnership allocated 87. 557% of its net business income to RCGW, despite RCGW holding only a 10% profits and loss interest. For the tax year ended April 30, 2005, the partnership consisted of only the three attorneys. The IRS reallocated the income for 2004 based on the partners' profits and loss interests and determined that the attorneys' distributive shares were subject to self-employment tax.

Procedural History

The IRS issued notices of final partnership administrative adjustment for the tax years ended April 30, 2004, and April 30, 2005. The partnership challenged these adjustments before the U. S. Tax Court, which consolidated the cases and reviewed them under de novo standard.

Issue(s)

Whether the special allocation of the partnership's net business income for the 2004 tax year was proper? Whether the income generated from the partnership's legal practice for the 2004 and 2005 tax years, and allocated to the attorney partners, is subject to self-employment tax?

Rule(s) of Law

A partner's distributive share of partnership income is determined by the

© 2025 SCOTUSreports.com. All rights reserved.

partnership agreement, provided it has substantial economic effect. If not, the share is determined according to the partner's interest in the partnership, considering factors such as capital contributions, profits and losses interests, cashflow distributions, and rights to capital upon liquidation. Net earnings from self-employment include a partner's distributive share of partnership income, with an exclusion for the distributive share of a limited partner under Section 1402(a)(13) of the Internal Revenue Code.

Holding

The special allocation of the partnership's net business income for the 2004 tax year was improper, and the IRS's reallocation based on the partners' profits and loss interests was sustained. The distributive shares of the partnership's net business income allocated to the attorney partners for the 2004 and 2005 tax years were subject to self-employment tax.

Reasoning

The court found no evidence of a partnership agreement supporting the special allocation for the 2004 tax year. The allocation to RCGW, which contributed minimally to the partnership's income, was inconsistent with the partners' economic interests. The court considered the partners' relative capital contributions, profits and loss interests, cashflow distributions, and liquidation rights, concluding that the IRS's reallocation was correct. Regarding self-employment tax, the court rejected the argument that LLP partners should be treated as limited partners under Section 1402(a)(13). The legislative history indicated that the exclusion was intended for passive investors, not for partners actively involved in the partnership's business, such as the attorney partners who generated income through their legal services.

Disposition

The court affirmed the IRS's reallocation of partnership income for the 2004 tax year and upheld the determination that the attorney partners' distributive shares were subject to self-employment tax for both the 2004 and 2005 tax years.

Significance/Impact

This case clarifies the IRS's authority to reallocate partnership income when special allocations do not reflect economic reality. It also establishes that partners in an LLP, who actively participate in the business, are not considered limited partners for self-employment tax purposes under Section 1402(a)(13). This decision impacts the tax treatment of income in professional partnerships and underscores the importance of aligning partnership allocations with economic substance.

© 2025 SCOTUSreports.com. All rights reserved.