Tigers Eye Trading, LLC v. Commissioner, 137 T. C. 67 (2011)

In Tigers Eye Trading, LLC v. Commissioner, the Tax Court held it had jurisdiction under TEFRA to uphold adjustments and penalties against a disregarded partnership, rejecting a challenge to its authority based on the D. C. Circuit's Petaluma II decision. The case clarified the Court's power to adjust partnership items and apply penalties at the partnership level when the partnership is deemed a sham, significantly impacting how tax shelters like the 'Son of BOSS' transaction are litigated.

Parties

Plaintiff (Petitioner): Tigers Eye Trading, LLC (dissolved prior to petition filing) and A. Scott Logan Grantor Retained Annuity Trust I (participating partner), with A. Scott Logan as Trustee. Defendant (Respondent): Commissioner of Internal Revenue.

Facts

The case involved a 'Son of BOSS' tax shelter transaction. A. Scott Logan, through Logan Trusts, purchased offsetting long and short foreign currency options and contributed them along with cash to Tigers Eye Trading, LLC, a Delaware LLC formed to engage in foreign currency trading but primarily used to generate tax losses. Tigers Eye was treated as a partnership for tax purposes but was later determined to be a sham with no economic substance. Logan claimed substantial losses on his 1999 tax return from the sale of property purportedly distributed by Tigers Eye, which were disallowed by the IRS in a Final Partnership Administrative Adjustment (FPAA). The FPAA adjusted partnership items to zero, including losses, deductions, capital contributions, and distributions, and applied accuracy-related penalties, including a 40% gross valuation misstatement penalty.

Procedural History

The case began with the IRS issuing an FPAA on March 7, 2005, to Tigers Eye's partners. Tigers Eye filed a petition in the U. S. Tax Court, with Sentinel Advisors, LLC, as the tax matters partner. Logan Trust I was granted leave to participate as a participating partner. A stipulated decision was entered on December 1, 2009, upholding the FPAA adjustments and penalties. Logan Trust I moved to revise the decision post-Petaluma II, arguing the Tax Court lacked jurisdiction over outside basis and related penalties. The Tax Court denied the motion to revise, finding it retained jurisdiction to enter the stipulated decision as written.

Issue(s)

Whether the U. S. Tax Court has jurisdiction under TEFRA to determine the applicability of penalties related to adjustments of partnership items when the partnership is disregarded for Federal income tax purposes?

Rule(s) of Law

Under sections 6233 and 6226(f) of the Internal Revenue Code, the Tax Court has jurisdiction over partnership items and the applicability of any penalty related to an adjustment to a partnership item in a partnership-level proceeding. Section 301. 6233-1T(a) and (c), Temporary Proced. & Admin. Regs. , extend this jurisdiction to entities filing as partnerships but determined not to be partnerships or to not exist for Federal tax purposes. Section 301. 6231(a)(3)-1, Proced. & Admin. Regs. , defines partnership items as those more appropriately determined at the partnership level.

Holding

The Tax Court held that it has jurisdiction under TEFRA to enter the stipulated decision as written, including upholding adjustments to partnership items and the applicability of penalties, even when the partnership is disregarded for Federal income tax purposes.

Reasoning

The Court's reasoning included several key points:

– The Court applied the TEFRA regulations, as mandated by Mayo Foundation and Intermountain, rather than following Petaluma II, which did not consider the regulations in its holding on outside basis.

– The Court determined that when a partnership is disregarded, items such as contributions, distributions, and the basis in distributed property are partnership items that can be adjusted to zero, and related penalties can be applied at the partnership level.

– The Court emphasized the logical and causal relationship between the determination that a partnership is disregarded and the disallowance of losses claimed on the sale of distributed property, justifying the application of penalties at the partnership level.

– The Court noted that the legislative history of TRA 1997 supports a broad reading of the Tax Court's jurisdiction over penalties related to partnership items.

– The Court rejected Logan Trust I's argument that Petaluma II limited its jurisdiction, finding that the decision was not binding precedent on the issue of penalties related to partnership items.

Disposition

The Tax Court denied Logan Trust I's motion to revise the stipulated decision, affirming the jurisdiction to uphold the adjustments and penalties as written in the decision entered on December 1, 2009.

Significance/Impact

The decision in Tigers Eye Trading, LLC v. Commissioner significantly impacts the litigation of tax shelters, particularly ‘Son of BOSS’ transactions, by clarifying the Tax Court’s jurisdiction to adjust partnership items and apply penalties at the partnership level when the partnership is disregarded. It reinforces the Court’s authority under TEFRA to address penalties related to partnership items, even when those items require adjustments to zero due to the partnership’s lack of economic substance. This case also highlights the complexity and ongoing challenges in applying TEFRA provisions to tax shelter cases, influencing future cases involving similar transactions.

