Bedrosian v. Commissioner, 143 T. C. 83 (2014) (U. S. Tax Court, 2014)

In a pivotal ruling on TEFRA partnership proceedings, the U. S. Tax Court in Bedrosian v. Commissioner clarified its jurisdiction over factual affected items, specifically tax attorney fees claimed by the Bedrosians. The court determined that such fees, not directly tied to partnership items but affected by them, are subject to deficiency procedures, thereby maintaining the court's jurisdiction. This decision reinforces the distinction between computational and factual affected items in tax law, affecting how tax assessments are handled post-TEFRA proceedings.

Parties

Plaintiffs: The Bedrosians, who participated in a Son-of-BOSS transaction through an investment in Stone Canyon Partners, LLC. Defendants: The Commissioner of Internal Revenue.

Facts

The Bedrosians were involved in a Son-of-BOSS transaction via their investment in Stone Canyon Partners, LLC, which was subject to the Tax Equity and Fiscal Responsibility Act (TEFRA) audit and litigation procedures. The IRS conducted an examination and issued a notice of final partnership administrative adjustment (FPAA) for the 1999 partnership taxable year, determining that the partnership was a sham. The Bedrosians did not file a timely petition in response to the FPAA, making all partnership items final. In a subsequent notice of deficiency for 1999 and 2000, the IRS disallowed a $525,000 deduction for tax attorney fees reported by the Bedrosians on their personal income tax return. This disallowed deduction was not directly related to the partnership items but was affected by the sham determination.

Procedural History

The IRS issued a notice of deficiency to the Bedrosians for the years 1999 and 2000, which included the disallowance of the $525,000 deduction for tax attorney fees. The Bedrosians filed a timely petition challenging the notice of deficiency. The U. S. Tax Court dismissed the partnership items and items resulting computationally from partnership adjustments, retaining jurisdiction over the deductibility of the professional fees. The Bedrosians later filed a motion for leave to file a motion for reconsideration of the court's findings regarding jurisdiction over the professional fees, which was denied as the court determined the deductibility of the fees to be a factual affected item subject to deficiency procedures.

Issue(s)

Whether the U. S. Tax Court has jurisdiction over the deductibility of professional fees claimed by the Bedrosians on their personal income tax return, which were not directly related to partnership items but were affected by the determination that the partnership was a sham.

Rule(s) of Law

Under the Tax Equity and Fiscal Responsibility Act (TEFRA), partnership items are determined at the partnership level and are final if not timely challenged. Nonpartnership items include items not classified as partnership items. Affected items are items affected by partnership items, and can be computational or factual. Computational affected items are not subject to deficiency procedures, while factual affected items are subject to such procedures. See sections 6230(a)(1) and 6230(a)(2)(A)(i) of the Internal Revenue Code.

Holding

The U. S. Tax Court held that it retains jurisdiction over the deductibility of the professional fees claimed by the Bedrosians, as these fees constitute a factual affected item subject to deficiency procedures.

Reasoning

The court's reasoning focused on the distinction between computational and factual affected items. The court referenced prior case law, including Domulewicz v. Commissioner, to establish that the deductibility of professional fees related to a partnership deemed a sham is an affected item. The court determined that the fees in question were not directly related to the partnership items but were affected by the partnership's sham status, necessitating a factual determination at the partner level. This factual determination required for the deductibility of the fees falls under the category of factual affected items, which are subject to deficiency procedures. The court emphasized that even if the factual determination might be undisputed by the parties, it remains a factual affected item, thereby retaining the court's jurisdiction over the issue.

The court also considered the Bedrosians' motion for reconsideration, applying the standards for granting such motions under Tax Court Rule 161 and Federal Rules of Civil Procedure rule 60(b). The court found no intervening change in controlling law that would justify reconsideration, as the determination of the professional fees as a factual affected item aligned with existing jurisprudence.

Disposition

The court denied the Bedrosians' motion for leave to file a motion for reconsideration, affirming its jurisdiction over the deductibility of the professional fees as a factual affected item subject to deficiency procedures.

Significance/Impact

The Bedrosian decision clarifies the scope of the U. S. Tax Court's jurisdiction over affected items in TEFRA proceedings, distinguishing between computational and factual affected items. This ruling has practical implications for taxpayers and the IRS in handling tax assessments post-TEFRA proceedings, particularly regarding the deductibility of professional fees related to partnerships deemed shams. The decision reinforces the need for partner-level factual determinations for certain affected items, potentially affecting the strategies of both taxpayers and the IRS in similar cases. The case also underscores the importance of timely filing in response to FPAAs, as failure to do so results in the finality of partnership items, limiting subsequent challenges.

