

(Leon).¹ For federal income tax purposes, a “partnership” with only one partner is not a partnership at all; rather, it is classified as an entity disregarded from its owner.²

The classification of the Art Partnership as “disregarded entity” means that for federal income tax purposes, Leon will be taxable on all of the Art Partnership’s income and will be treated as owning all of the Art Partnership’s assets. Accordingly, any distributions of property by the Art Partnership to Leon will not be subject to the typical partnership tax rules relating to basis adjustment or gain recognition.³

New York State sales tax consequences

Based on the New York Tax Law (the “Tax Law”) and the New York Code of Rules and Regulations (the “NYCRR”), Leon’s contribution of art to the Art Partnership should not be subject to New York State sales tax. Section 1105(a) of the Tax Law provides that a sales tax is imposed on “[t]he receipts from every retail sale of tangible personal property.” Section 1101(b)(4)(iv) of the Tax Law, however, provides that “[t]he term retail sale does not include...[t]he contribution of property to a partnership in consideration for a partnership interest therein.” Section 526.6(d) of the NYCRR states that “[a] partner’s contribution is the property valued in money or the monetary amount he contributes to the firm for commencing or carrying

¹ See Priv. Ltr. Rul. 200102037 (LLC whose members are an individual and a grantor trust owned by such individual within the meaning of § 671 is a disregarded entity); See also Rev. Rul. 77-402, Priv. Ltr. Ruls. 9515006, 9515008, 9515009, 9515013; FSA 200035006.

² See *Treas. Reg.* § 301.7701-3(b), which provides that “unless the entity elects otherwise, a domestic eligible entity is (i) a partnership if it has two or more members; or (ii) disregarded as an entity separate from its owner if it has a single owner.”

³ For example, if at some point the Art Partnership were to decide to distribute the art to the Trust, the “mixing bowl” and “disguised sale” rules of §§ 704(c)(1)(B) and 707(a)(2)(B) of the Internal Revenue Code would not be applicable.

on the business whether at the commencement of the business or later. Contributions of property are not subject to sales or use tax.”⁴

Additionally, it should be noted that the Tax Law and the NYCRR provide an exemption from sales tax for distributions of partnership property to a partner, in whole or partial liquidation of the partner’s partnership interest.⁵ Accordingly, should it make sense in the future for the art to be held by a partner, the Art Partnership should be able to distribute the art to the partner free of sales tax, provided that the partner’s capital account is correspondingly reduced.⁶

⁴ Note that § 11-2001(b)(4)(ii) of the New York City Administrative Code contains provisions relating to partnership contributions that are identical to those in § 526.6(d) of the NYCRR. Accordingly, Leon’s contribution of the art to the Art Partnership should be exempt from both New York City and New York State sales tax.

⁵ Section 1101(b)(4)(iv) of the Tax Law provides that “[t]he term retail sale does not include...[t]he distribution of property by a partnership to its partners in whole or partial liquidation.” Section 526.6(d)(3) of NYCRR states that “[t]he liquidation of a partnership is the return, complete or partial, of partnership capital to the partners. In a liquidation, a partner’s interest is diminished by the value of the property distributed to him. The distribution of tangible personal property pursuant to a liquidation is not a taxable sale.”

⁶ Note that there appear to be no authorities suggesting that the consequences described in the text above should be any different where the distributed property had originally been contributed by a partner. In fact, in *Duracast Contracting Corp.*, TSB-H-81(57)S (N.Y. State Tax Comm. 1981), the New York State Tax Commission indicated that a distribution of property followed by an *immediate* re-contribution of the same property to a new entity would not be subject to sales tax. Although *Duracast* dealt with transactions between a corporation and its shareholders, the court based its analysis on § 1101(b)(4)(iv) of the Tax Law, which provides exemptions from sales tax for contributions to and distributions from corporations that parallel those described above with respect to partnerships.

Clapp, Ada

From: Kirschner, Elyse [REDACTED]
Sent: Friday, January 15, 2010 3:42 PM
To: Clapp, Ada
Cc: [REDACTED]; McCaffrey, Carlyn
Subject: RE: Leon Black

Dear Ada:

If the partnership earns income from the investment assets contributed by the trust, couldn't it make a pro rata distribution of that income to its partners (Leon and the trust)? We wouldn't want the partnership to distribute to Leon a chunk of the assets contributed by the trust within the first 2 years (to avoid an argument that Leon made a disguised sale of the art for sales tax purposes). But I think a pro rata distribution of income would be OK.

Elyse

Elyse G. Kirschner, Esq.
Weil, Gotshal & Manges LLP
767 Fifth Avenue
New York, New York 10153
Telephone: [REDACTED]
Facsimile: [REDACTED]

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From: Clapp, Ada [REDACTED]
Sent: Friday, January 15, 2010 2:14 PM
To: Kirschner, Elyse
Cc: [REDACTED]; McCaffrey, Carlyn
Subject: Re: Leon Black

Since it appears that not all of the distributions coming into the 2006 Trust will be required to be distributed out to Leon (because they do not represent trust accounting income from Relevant Companies") these amounts could be contributed to the art partnership. That way Leon can diversify his art portfolio and get some liquidity in a couple of years without having to rely on discretionary distributions from a trust to Debra. I agree that it is better planning for Leon to just forgo the mandatory distributions from the Relevant Companies but then what does he do about cash flow for the 2 years he can't access cash from the art partnership?

Ada Clapp
Sr. Vice President
Wealth Strategist
U.S. Trust Bank of America Private Wealth Management
114 West 47th Street
New York, NY 10036

[REDACTED]

From: Kirschner, Elyse <[REDACTED]>
To: Clapp, Ada
Cc: Eileen Alexanderson <EAlexanderson@[REDACTED]>; McCaffrey, Carlyn <[REDACTED]>