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Legal Ruling 2021-01 — When the Tail Wags the Dog

by Ted Tourian

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In this article, Tourian examines the FTB's Legal Ruling 2021-01, which addresses situations in which a passthrough entity serves as a holding entity of another passthrough entity. He argues that the ruling muddles unitary analysis for passthrough entities when it ignores that LLC members are required to file whether they are general or limited partners for tax purposes for federal and California tax purposes.

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The California Franchise Tax Board released Legal Ruling (LR) 2021-01 (Oct. 25, 2021) on how to apply unitary business principles to passthrough entities, such as partnerships, S corporations, and limited liability companies. It discusses situations in which a passthrough entity serves as a holding entity of another passthrough entity but muddles unitary analysis for passthrough entities when it ignores that LLC members are required to file whether they are general or limited partners for tax purposes for federal and California tax.

This article first describes the different entity classifications and their respective tax filing requirements. It then describes the difficulty of classifying LLC members as general or limited partners but notes its importance for federal and state tax purposes. Next it describes how the classification of a general partner or limited partner affects the doing business and unitary determinations for partnerships, but explains how these classifications are omitted by the FTB regarding LLCs.

The reason the FTB ignores the classification of general or limited partner for LLCs is that it is beholden to its prior letter rulings, 2014-01 and 2018-01, which treat all LLC members equally to impose the $800 minimum franchise tax on all LLC members. Ignoring the general/limited partnership classification for LLC members could skewer unitary analysis. Finally, shoehorning the new concept of passthrough entity holding company (PEHC), while ignoring the partnership classification for LLC members, creates disparate unitary treatment between LLCs and partnerships.

Entity Classifications and Filing Requirements

Holding Company

Holding companies, like any other corporation, are separate from their owners and their subsidiaries, for both legal and tax purposes. A holding company may be entirely passive or may provide management and oversight functions to its subsidiaries. In either case, the holding company's activities are generally limited. There are no unique unitary tests for holding companies.[1] And like any other corporation, they are required to file California Form 100.[2]

[1] Multistate Audit Technical Manual (MATM), section 3080, "Unitary Combination of Holding Companies" (rev. Aug. 2019).

[2] 2021 Instructions for Form 100, Corporation Tax Booklet, "General Information" (rev. Feb. 2022).

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Partnership

A partnership is an entity though which two or more persons carry on a trade or business, with each contributing money, property, labor, or special skills and each expecting to share in the profits and losses from the business activity.[3] IRC section 761(a) provides the federal definition of a partnership. RTC section 17851 conforms to subchapter K.

Whether a person is classified as a general or limited partner is a matter of election for federal and California tax purposes.[4] This is reflected in FTB Form 565, lines 21a through 21b, on which partners in a partnership classify whether they are general or limited partners.[5]

Limited Liability Company

An LLC with at least two members is classified as a partnership for federal income tax purposes, unless it affirmatively elects out of that classification.[6] An LLC can choose to classify itself as a corporation or a partnership for both federal and state purposes.[7] If an LLC chooses to be a partnership, then it will report income in the same manner as other partnerships.[8]

An LLC structure is different from partnerships. A person is an LLC member-manager if that member has the right to participate in the management and conduct of the LLC's business. For an LLC that is designated as a member-managed LLC in its articles of organization, all members of the LLC will be member-managers. For an LLC that is designated as a *manager*-managed LLC in its articles of organization, only those persons who are both members of the LLC *and* are designated as a manager in the LLC's operating agreement (or elected as managers by the LLC members under the operating agreement) will be member-managers.

The GP and LP Classification Conundrum

For LLCs classified as partnerships for federal tax purposes, an important issue is whether members should be imputed general or limited partnership status.[9] This issue has been analyzed in similar contexts such as LLPs.

For example, TAM 9728002 held that the partnership's trade or business should not be imputed to limited partners, but only to general partners, in connection with the attempted deduction of legal fees incurred by a limited partner in a lawsuit against the general partner, thereby resulting in an IRC section 212 itemized deduction rather than an IRC section 162 above-the-line deduction. The classification of whether a partner is a general or limited partner affects a taxpayer's income.[10]

The issue extends to other IRC provisions. For instance, section 1401 generally subjects an individual to self-employment tax on his or her net earnings. Section 1402(a) generally defines net earnings from self-employment for purposes of determining a tax base. Section 1402(a)(13) provides an exception to the distributive shares of limited partners, except for guaranteed payments.[11]

Determining who is a limited partner for self-employment tax purposes can be difficult. In *Renkemeyer, Campbell & Weaver LLP*[12] the Tax Court ruled that attorney partners in an LLP were not

[3] Cal. Rev. & Tax Code section 17008 provides the structures through which a partnership can exist in California. A partnership includes a syndicate, group, pool, joint venture, or other unincorporated organization through which any business, financial operation, or venture is carried on and that is not a corporation, a trust, or an estate.

[4] Cal. Rev. & Tax Code section 23038(b)(2).

[5] 2021 Instructions for Form 565, Partnership Return of Income, "Analysis — Schedule K (565) Only" (rev. Feb. 2022), provides: "Line 21a through Line 21b(2) — For the instructions for line 21a through line 21b(2) of Schedule K (565), see the instructions for federal Schedule K (1065), Analysis of Net Income (Loss)."

[6] Reg. 301.7701-3(b)(1)(i); IRS Publication 3402, at 3 (rev. Mar. 2020).

[7] 2021 Instructions for Form 100, Corporation Tax Booklet, "X. Limited Liability Companies (LLCs)" (rev. Feb. 2022).

[8] 2021 Instructions for Form 568, Limited Liability Company Tax Booklet, "Analysis (Schedule K (568) only)" (rev. Feb. 2022), provides: "Line 21a and Line 21b — See the federal instructions for Schedule K (1065), Analysis of Net Income (Loss)."

[9] Shop Talk, "Are LLC Members GPs or LPs for Federal or State Tax Purposes?" 98 *J. Tax* 62 (Jan. 2003).

[10] 2021 Instructions for Form 565, Partnership Return of Income, "General Information" (rev. Feb. 2022), states: "Partners should follow federal reporting requirements as detailed in federal Form 1065, U.S. Return of Partnership Income, and federal Form 4797, Sales of Business Property."

[11] Section 1402(a)(13) states: "There shall be excluded the distributive share of any item of income or loss of a limited partner, as such, other than guaranteed payments described in section 707(c) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services."

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

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limited partners for purposes of section 1402(a)(13). The taxpayer LLP partners argued that the limited partner exemption should apply because (1) the LLP organizational documents designated their interests as limited partnership interests and (2) they enjoyed limited liability under state law. The Tax Court disagreed, reaching the result that would have been required under the temporary regulations.[13]

Imputing general or limited partner status to an LLC member is not limited to the federal level. For instance, New York generally excludes from its taxing jurisdiction out-of-state corporate limited partners that are not engaged, directly or indirectly, "in the participation in or the domination or control of all or any portion of the business activities or affairs of the partnership." The regulations provide multiple presumptions regarding which corporate limited partners might be considered so engaged, notwithstanding the particular facts.[14]

New York Advisory Opinion No. TSB -A-02 (14)C analyzed 20 NYCRR section 1-3.2(a)(6).[15] The facts pertained to whether member-managers or members of an LLC should be treated as limited or general partners. The analysis was facts and circumstances but ultimately defaulted to the classification of general or limited partner.[16]

Oregon imputes general or limited partner status on LLC members for purposes of taxing a nonresident's gain or loss from the sale, exchange, or disposition of an interest in an LLC operating in the state is Oregon source income.[17]

Doing Business and Unity — When the GP and LP Classifications Matter

This section compares how the FTB considers the general/limited partner distinction in determining whether a partner is doing business in California or is unitary with its tiers, while ignoring the general/limited partner classification for LLC members.

		Is the GP/LP distinction considered for determining:	
		Doing Business	Unity
Entity	Partnership	✔	✔
	LLC	Ignored	Ignored

Partnership Doing Business Standards

Cal. Rev. & Tax Code section 23101 provides the general provisions for a person doing business in California. General partners are generally deemed to be doing business in California because a general partner is considered doing business where the partnership operates.[18] However, limited partners are generally not considered to be doing business in California simply by owning a limited partnership interest in the state.[19]

For instance, in *Appeal of Amman & Schmid Finanz AG*,[20] the issue was whether a limited partner was doing business in California under

[13] *Id.* at 148 provides:

> When L.L.P.s (and limited liability companies) began to be frequently used, it was determined that there needed to be a definition of "limited partner" for purposes of the self-employment tax. In 1997 the Secretary issued proposed regulations which were intended to do just that. See sec. 1.1402(a)–2, Proposed Income Tax Regs., 62 Fed. Reg. 1704 (Jan. 13, 1997). The proposed regulations ignited controversy. As a result, Congress enacted legislation which provided that "No temporary or final regulation with respect to the definition of a limited partner under section 1402(a)(13) of the Internal Revenue Code of 1986 may be issued or made effective before July 1, 1998." Taxpayer Relief Act of 1997, Pub. L. 105–34, sec. 935, 111 Stat. 882.

[14] 20 NYCRR 1-3.2(a)(6)(i) and (ii). The draft regulations for New York are substantially the same as in this section.

[15] *Id.*

[16] New York Advisory Opinion No. TSB-A-02 (14)C (July 9, 2002) states:

> If the activities of a corporate member of an LLC that is treated as a partnership for New York State tax purposes are similar to the activities of a general partner of a partnership, such corporate member will be treated like a general partner. However, if the activities of a corporate member of an LLC are similar to the activities of a limited partner of a partnership, such corporate member will be treated like a limited partner. See Stone Commodities Corp, Adv Op Comm T&F, December 4, 1997, TSB-A-97(26)C and FGIC CMRC Corp, supra.

[17] Or. Admin. R. 150-316-0171(2)(f).

[18] *Appeal of Custom Component Switches Inc.*, 77-SBE-009 (Feb. 3, 1977); *Appeal of H.F. Ahmanson & Co.*, 65-SBE-013 (Apr. 5, 1965).

[19] Cal. Rev. & Tax Code section 23101(d) may provide a situation in which California may assert jurisdiction on a limited partner whose distributive shares exceed the doing business threshold amounts found under section 23101(b). It should be noted that for purposes of section 23101(d) the term "passthrough entities" means a partnership or an S corporation. Section 23101(d) did not mention LLCs. The assumption is that LLCs filing as partnerships *should* be treated as partnerships, for tax purposes.

[20] *Appeal of Amman & Schmid Finanz AG*, 96-SBE-008 (Apr. 11, 1996).

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section 23101.[21] *Amman* ruled that nexus is not accorded because a person is a limited partner.[22] The FTB ruled that the taxpayers were not doing business in California, where their partnership interests were characterized as a passive investment.

LLC Doing Business Standards

The FTB imposes nexus under section 23101 for all members of an LLC treated as a partnership and ignores whether an LLC is member-managed or manager-managed or is classified as a general or limited partner for federal and California purposes.

LR 2014-01 provides that: (1) California follows the federal entity classification system, (that is, the check-the-box regulations); and (2) if an LLC is classified as a partnership for federal income tax purposes, both the LLC and its members should be subject to the same legal principles that apply to any partnership in determining nexus. The FTB then provides six examples that illustrate when an LLC and its corporate members have a franchise tax or LLC filing fee.

LR 2014-01, situation 5, provides that an LLC's classification as member-managed or manager-managed is irrelevant for determining whether a corporate member is subject to an income tax reporting and payment obligation. The FTB relies on the principle that every LLC member that chose not to manage the LLC was participating in management because the choice to not participate is a management decision in and of itself.[23] Further, LR 2014-01, situation 5 is particularly important in cases in which the FTB ignored whether an LLC member would be a limited or general partner for federal tax purposes.

The California Court of Appeal disagreed with LR 2014-01 in *Swart Enterprises*.[24] In *Swart*, the court held that an out-of-state taxpayer was not doing business in California because it held a small (0.2 percent), non-managing-member interest in a manager-managed LLC investment fund. The court reasoned that the taxpayer was not doing business in the state because it had no interest in specific property of the LLC, was not personally liable for its obligations, played no role in its management and had no right to, and could not act as an agent for the LLC or bind the LLC in any way.[25] In essence, the court found that the taxpayer in *Swart* was more akin to a limited partner than a general partner, and the law is clear that the doing business status of a limited partnership is not attributed to a partnership's limited partners.

However, the FTB doubled down on LR 2014-01 with LR 2018-01, in which the FTB tried to limit *Swart* to its facts. The game changer for the FTB was that the fictional taxpayer LLC member in LR 2014-01, situation 5, held a 15 percent interest rather than a 0.2 percent interest.[26] Once again, the FTB ignored whether an LLC member would be treated as a general or limited partner for tax purposes.

[21] *Amman* states: "Appellants' position is that 'doing business' is defined by the Bank and Corporation Tax Law as 'actively' engaging in any transaction for the purpose of financial or pecuniary gain or profit (Rev. & Tax. Code, §23101). Appellants contend that, while that definition does not require the conduct of a regular course of business, it nevertheless does require active participation in the profitseeking activity, and limited partners are necessarily passive or inactive members of the partnership."

[22] *Amman* states: "As stated in the opinion, 'On the basis of these rules, this board is unable to conclude that appellants are doing business here individually *simply because* they have interests as limited partners in limited partnerships which are engaged in business here.' 'Simply because' implies the ownership interest is not enough to give a limited partner nexus in California because of their ownership in California." (Emphasis added).

[23] LR 2014-01 provides:
If an LLC is treated as a partnership for tax purposes, both the LLC and its members, are subject to the same legal principles applicable to any partnership. Thus, if an LLC classified as a partnership for tax purposes is "doing business" in California under Section 23101, the members of the LLC are themselves "doing business" in California. This is true even in the case of "manager-managed" LLCs. Members of LLCs generally have the right to participate in the management of the business. Part of that power necessarily includes the right to delegate the power to manage the business in favor of a manager, and the power to revoke that delegation at any time. This analysis is not affected by whether or not members participate in the management of an LLC or appoint a manager to do so because the members' rights to participate in the management of the business arise out of the statutory relationship between an LLC and its members. Partners are considered co-owners of the partnership enterprise and the partnership acts as a conduit through which the enterprise is operated.

[24] *Swart Enterprises Inc. v. Franchise Tax Bd.*, 7 Cal.App.5th 497 (2017).

[25] *Swart*, 7 Cal.App.5th, at 507-513.

[26] LR 2018-01 states: "Please note that Member J's 15 percent membership interest in LLC I greatly exceeds the taxpayer's 0.2 percent membership interest in the *Swart* Court of Appeal decision."

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Partnership Unitary Standards

Cal. Code regs. tit. 18, section 25137-1(a), provides that the determination of a unitary business is made under established principles, which turns on the facts of each case. A unitary business is generally established by the presence of unity of ownership; unity of operation as evidenced by central accounting, purchasing, advertising, and management divisions; and unity of use in a centralized executive force and general system of operation.[27] However, the BOE held that a corporate partner can be unitary if it owns less than a 50 percent interest in the partnership[28]

Gasco Gasoline[29] provides that, absent rare circumstances, it is unlikely that a limited partnership interest will be found unitary despite evidence that unitary factors may exist.

LLC Unitary Standards

Like partnerships, determining whether an LLC is unitary with its members is a facts and circumstances analysis. Membership interests are analogous to partnership interests or to stock in a corporation.[30] The FTB further recognizes that every LLC member is an agent of the LLC, unless the articles of organization or operating agreement restrict the scope of the member's authority.[31] The FTB provides that if an LLC elects to be treated as a corporation, then corporate rules for unity should be applied. If an LLC elects to be treated as a partnership, then partnership rules should be used to determine whether an LLC is unitary.

LR 2021-01 recognizes that some LLC passthrough entities are like holding companies. It provides that "traditional tests for unity are not an exact fit in the context of pass-through entity holding companies." Recognizing that these LLCs are unique, the FTB completely ignores how LLC members are required to file as a general or limited partner at both the federal and state level. Rather, the FTB uses prior LRs 1995-7 and 1995-8 as a basis of analogizing these entities to holding companies.

Statutory Silence — How the Tail Started to Wag the Dog

LR 2021-01 covers several situations pertaining to passthrough LLCs while purposely ignoring the mandatory filings concerning how an LLC member would classify itself — as either a general or limited partner — for tax purposes.

However, LR 2021-01, situation 5, provides a clear example of the FTB recognizing when a partner is a general or limited partner for purposes of determining a unitary relationship between partnerships. Under the doctrine of statutory silence,[32] it is apparent that the FTB meant to ignore how LLC members in passthrough entities classify themselves as either a general or limited partner for tax purposes. As discussed above, these filings are required. Taxpaying LLC members in a passthrough entity are *required* to classify themselves.

The logical conclusion is that LR 2021-01 is beholden to the FTB's litigating positions in LRs 2014-01 and 2018-01, in which the FTB tries to impute its doing business standard on every LLC member. The minute the FTB recognizes that an LLC member can be a limited partner, the board fears it will lose its ability to collect an $800 doing business fee from just about every LLC member. And it is probably right. Most taxpayers just want to take their steaks home, pay the $800, and call it a day. Not everyone is willing to fight like Swart.

[27] *Butler Bros. v. McColgan*, 315 U.S. 501 (1942).

[28] *In the Appeal of Saga Corp.*, 82-SBE-102 (June 29, 1982).

[29] *Appeal of Gasco Gasoline Inc.*, 88-SBE-017 (June 1, 1988).

[30] MATM, section 3087, "Unitary Combination of Limited Liability Companies (LLCs)" (rev. Aug. 2019).

[31] *Id.* states: "Unless the articles of organization or operating agreement restrict the scope of the member's authority, every member of an LLC is an agent of the LLC for the purpose of its business or affairs. (California Corporation Code section 17157.) When an agent conducts activity within the scope of his authority or which is subsequently ratified, the agent's principal is considered to have conducted that activity. (California Civil Code sections 2295 and 2330.)."

[32] *Director, OWCP v. Newport News Shipbuilding Co.*, 514 U.S. 122 (1995) (agency in its governmental capacity is not a "person adversely affected or aggrieved" for purposes of judicial review). *See also United States v. Bestfoods*, 524 U.S. 51, 62 (1998) ("Against this venerable common-law backdrop, the congressional silence is audible."); *Elkins v. Moreno*, 435 U.S. 647, 666 (1978) (absence of reference to an immigrant's intent to remain citizen of foreign country is "pregnant" when contrasted with other provisions of "comprehensive and complete" immigration code); *Meyer v. Holley*, 537 U.S. 280 (2003) (ordinary rules of vicarious liability apply to tort actions under the Fair Housing Act; statutory silence as to vicarious liability contrasts with explicit departures in other laws).

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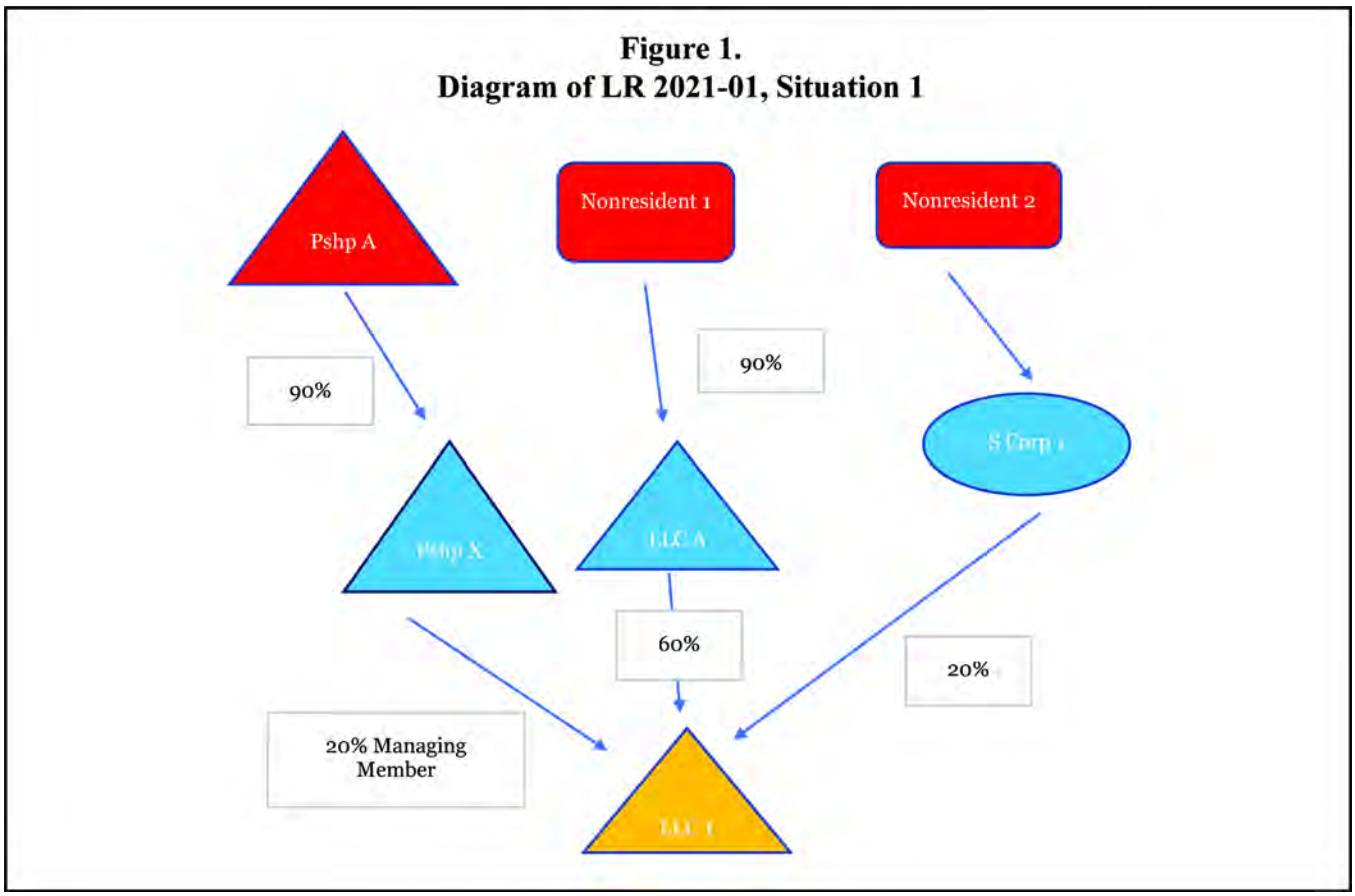

The second inference from this statutory silence is that taxpayers are entitled to rely on the FTB's position of ignoring the general/limited partner classification in determining unity for LLC members of a passthrough entity, and the FTB is bound to ignore it too.[33] However the FTB's purposeful silence does not require a taxpayer to ignore the general/limited partner classification. By letting the tail wag the FTB dog, did the FTB just whipsaw itself?

The Passthrough Holding Company — Continue Letting the Tail Wag the Dog or Embrace the GP/LP Dichotomy

Ignoring the general/limited partnership classification for LLC members could skewer unitary analysis. The FTB tried to ignore this necessary filing classification by shoehorning the analysis under *PBS Building Systems*,[34] which applied to holding corporations, in which 50 percent ownership is a requirement.

In LR 2021-01, situation 1, the FTB provides a tiered ownership structure between several partnerships, LLCs, S corps, and nonresidents. The example introduces the concept of a PEHC.[35] LLC 1 is owned by Partnership X with a 20 percent interest, LLC A with a 60 percent interest, and S Corp 1 with a 20 percent interest. All LLC 1 owners are holding companies with no operations

[33] *Appeal of Union Carbide Corp.*, 84-SBE-057 (Apr. 5, 1984).

[34] *Appeal of PBS Building Systems Inc. and PKH Building Systems Inc.*, 94-SBE-008 (Nov. 17, 1994).

[35] LR 2021-01 introduces the concept of a PEHC:
Therefore, in instances where a pass-through entity holding company holds less than a controlling interest in an operating entity, the holding company can still be unitary with the operating entity, to the extent of its ownership interest in the entity. This is because pass-through entities need not hold more than fifty percent of an entity to be unitary with that entity. (FN 53 omitted) As long as unitary indicia, as discussed above, exist, a pass-through entity holding company can be unitary with an operating entity. If a pass-through entity holding company provides value and support to the operating business, it will be properly treated as unitary with that business.

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or employees of their own and no assets other than an ownership interest in LLC1. All LLC 1 owners have a proportionate share of votes in relation to their ownership interests. Partnership A owns 90 percent of PSHP X, which is the managing member of LLC 1. The general partners and employees of PSHP A act on behalf of PSHP X to manage the day-today operations of LLC 1.

The FTB ruled that S Corp 1 and LLC 1 are not unitary, when S Corp 1 does not participate in the day-to-day operations of LLC 1, and when it does not have a controlling interest in LLC 1. Contrasting the unitary determination between S Corp 1 and Partnership X, the FTB ruled that LLC A and LLC 1 are unitary, when it focused on the unitary analysis of a holding company as found under *PBS*,[36] which is discussed more under LR 1995-8. The analysis focused on the fact that LLC A had three out of five votes for LLC 1. What if both LLC A and S Corp 1 owned LLC 1 equally, when both became minority owners of LLC 1?

The FTB's reliance on *PBS* would no longer apply. *PBS* applies to holding companies, for whom majority ownership is a requirement for determining unity between corporations sharing the same trade or business. Unlike *PBS*, *Saga* provides that a controlling interest is not a requirement for determining unity for partnerships. LLC A and S Corp 1 could control LLC 1's policy decisions some of the time.

One factor that should be used is the general/limited partner classification that LLC A and S Corp 1 would be required to file. However, were the FTB to look at this factor, there would be two unintended consequences.

First, the FTB's position in LR 2021-01, situation 1, in which the board initially found S Corp 1 not unitary with LLC 1, would have to be reevaluated to incorporate the general and limited partner classification in its analysis.

Second, recognizing the partnership classification for LLC A and S Corp 1 as minority owners could cause the FTB's house of cards to fall pertaining to LR 2018-01. As a recap, LR 2018-01 held that a taxpayer who owned a 20 percent passive interest in LLC was doing business in California. Accepting a limited partner status in this situation would possibly derail the FTB money train from the LLC fees.

Situation 4 — Getting Lost in the Shuffle

LR 2021-01, situation 4, provides a situation in which the concept of the PEHC takes flight. Preexisting concepts of analyzing unitary relationships between partnerships and other passthrough entities become muddled, as the PEHC concept is shoehorned into the passthrough entity discourse.

In situation 4, it is unclear what type of legal entities PSHP W, Y, and Z are. For purposes of this analysis, the assumption is that they are either general partnerships or LLCs treated as partnerships. The reason for this assumption is that LR 2021-01 starts by saying that it will only be analyzing passthrough entities.[37] Further, these entities have PSHP in their names, denoting partnerships. However, situation 4 describes these entities as "Company." I am assuming that Company refers to the FTB's introduction of a new type of entity, the passthrough holding company, discussed throughout LR 2021-01.

Under LR 2021-01, situation 4, the FTB provides a tiered ownership structure between three partnerships. PSHP W, is a real estate company that holds an 85 percent interest in PSHP Y, which does not have any employees. Finally, PSHP Y holds a 10 percent interest in PSHP Z, whose business activities are those of a software developer.

The ruling provides that none of the partnerships are unitary with one another. However, by not classifying the entities, and not attributing a general or limited partner classification, the FTB used holding company rules from *PBS* and LR 1995-7 to argue that PSHP W and Y are not unitary. But established principles of unity would most likely find that the relationship between PSHPs W and Y would most likely be unitary, especially if PSHPs W and Y are classified as partnerships.

[36] 94-SBE-008.

[37] LR 2021-01 states: "ISSUE: Whether, in a series of differing situations, pass-through entity holding companies are unitary with other pass-through entities."

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Figure 2.
Change of Ownership Structure for LR 2021-01, Situation 1

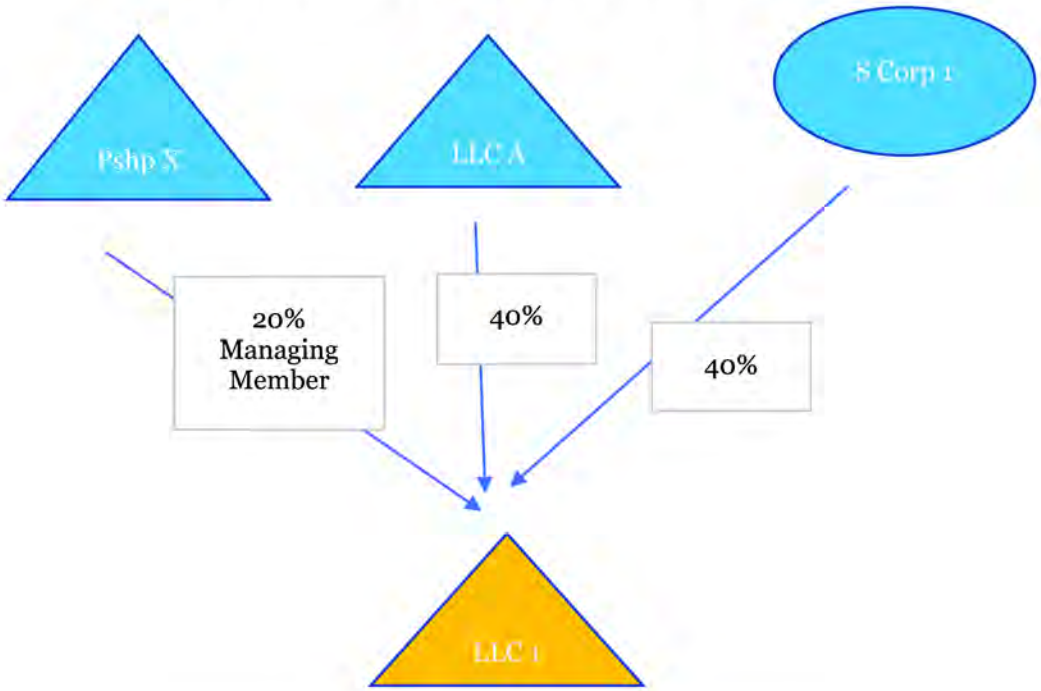
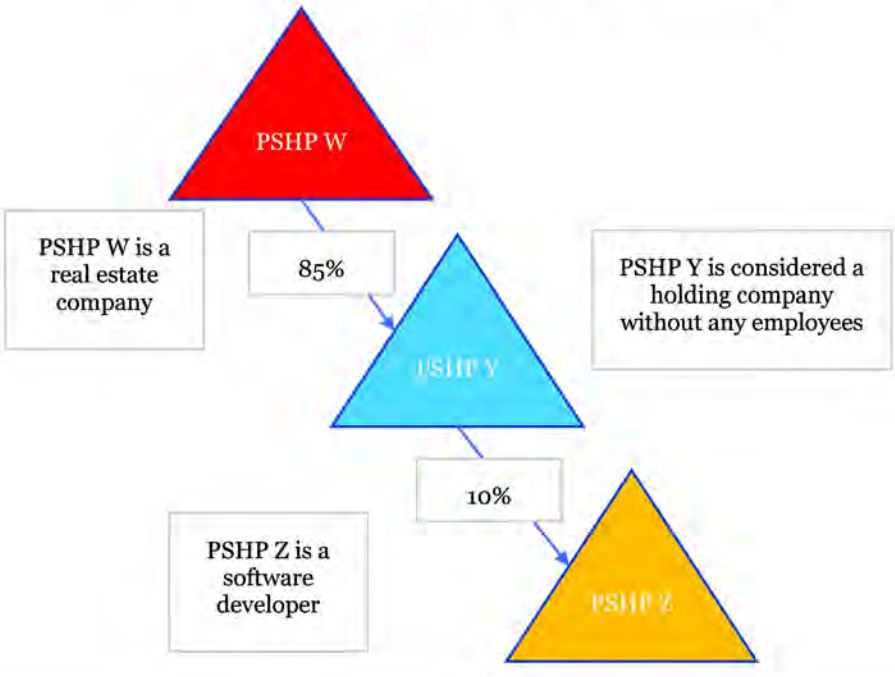


Figure 3.
Ownership Structure of LR 2021-01, Situation 4



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For instance, in LR 1991-1, section 14, Partnerships as a Concerted Group, the FTB said that a general partner that owned a majority interest in an underlying partnership automatically met the "unity of ownership" requirement for a determination of unity.[38] It is difficult to find any case law providing that a general partner owning a majority interest in a partnership is not unitary, especially when, based on the facts, the underlying partnership would presumably rely on the general partner for its entire executive force and for providing all centralized management decisions.[39]

By not defining the entities listed in LR 2021-01, situation 4, and their classifications, there is an argument that taxpayers can now elect whether they want to be unitary with their lower-tiered PEHC by choosing to classify as a general partnership for unity, and anything but a general partnership for non-unity.

Conclusion

LR 2021-01 is a step in the right direction by the FTB in trying to clarify unitary relationships between passthrough holding entities. However, the analysis is beholden to prior LRs 2014-01 and 2018-01, in which the FTB does not acknowledge the required classification of general or limited partnership status for LLC members of LLCs electing to be partnerships. As such, LR 2021-01 demonstrates how the $800 LLC fee wags the multistate dog. ■

[38] LR 1991-1, Section 14: Partnerships as a Concerted Group states: "If a corporation holds a more than a 50% interest in a general partnership, and the partnership agreement does not assign voting power to another partner, unity of ownership exists between the more than 50% corporate partner and the corporation held by the partnership." LR 1991-1 was published after *Saga*, which was published in 1982. As such, even though unity of ownership was not required for partnerships in 1991, LR 1991-1 provides that unity of ownership is still factored in the determination of unity for partnerships.

[39] *Butler Bros.*, 315 U.S. 501.

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