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Kirkland Alert

Tax Court Addresses Scope of “Limited Partner Exception” to Self-Employment Tax in Context of Management Company Income

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On November 28, 2023, the U.S. Tax Court issued an [opinion](#) in *Soroban Capital Partners LP v. Commissioner*, addressing the threshold legal issue of the scope of the “limited partner exception” to self-employment taxes in respect of an individual limited partner’s distributive share of management company income.

The Tax Court ruled against the taxpayer (and in favor of the Internal Revenue Service (IRS)) on this threshold issue, holding that state law limited partners are not *per se* entitled to the exception. According to the court, Congress intended for the limited partner exception to apply to earnings of an investment nature allocated to passive (rather than active) investors. To determine whether the earnings allocated to limited partners are of an investment nature, the court concluded it must conduct an inquiry into the functions and roles of the limited partners.

The court had to decide the appropriate legal standard before addressing this factual question, so it did not make a final determination as to whether the limited partners in the management company qualified (in whole or in part) for the limited partner exception. The IRS argued that a trial is necessary to develop these facts.

The taxpayer may appeal this decision to the U.S. Court of Appeals for the Second Circuit, but the procedural course and timing are unclear at this time.

If you have any questions about this decision, please reach out to a member of your Kirkland Tax team.

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