

PROFESSIONAL SERVICE ORGANIZATIONS: A REPLY

In applying the term "association" as used in section 7701(a)(3), Mr. Thies argues that we can find guidance in a "largely overlooked" cranny of the law: the "common law association."¹ Asserting that this form of organization was characterized by centralized management and continuity of life, but not by limited liability or transferability of interests, Mr. Thies concludes that the first two characteristics alone are the only proper criteria of association status. The test, in other words, is whether the organization under examination resembles a "classic common law association," not whether it resembles a corporation; and this in turn means that centralized management and continuity of life are sufficient (and, evidently, necessary) to confer association status under section 7701(a)(3). Mr. Thies then asserts that "virtually all" new-style professional association and corporation statutes satisfy these criteria.

Although the final step in Mr. Thies' ingenious argument is independently open to debate, I wish to examine here only his central thesis—that the term "association" in section 7701(a)(3) refers to what he calls "classic common law associations." If this theory is correct, Mr. Thies is right in asserting that the courts, Treasury lawyers, private practitioners, and commentators have been repeatedly wrong in their understanding of this area. It would also follow, although Mr. Thies does not explicitly press this corollary to his theory, that the new-style professional association and corporation statutes which evoked the entire debate were unnecessary: In his view, any professional group that so desired—or even a solo practitioner²—could have organized a common law association as a means of qualifying for corporate tax status. If Mr. Thies' novel argument is wrong, however, the claim of a new-style professional association or corporation to association status must continue to rest on the familiar arguments that have been offered by other commentators on this subject.

The validity of the central point in Mr. Thies' argument can be conveniently tested by asking how a group of taxpayers who wanted to organize a common law association could go about doing so. His answer, I take it,

¹ Thies, *Professional Service Organizations: A Comment*, 24 TAX L. REV. 291 (1969), commenting on my article, *Professional Service Organizations: A Critique of the Literature*, 23 TAX L. REV. 429 (1968). See also an earlier statement of Mr. Thies' views, *An Open Letter to a Former Secretary of the Treasury*, 46 TAXES 529 (1968).

Though I am pleased to have Mr. Thies' concurrence in my criticism of some other comments on this subject, he overstates my view in characterizing these arguments as "overly polemical in the worst sense of the term." I used the term "polemical" as a synonym for disputatious or argumentative, and included my own 1961 article in the list of "polemical literature." See 23 TAX L. REV. at 429.

² Although Mr. Thies seems to be confident that a one man association would be recognized as such by the courts, other commentators have been more cautious. The observation in Bittker & Eustice, *Federal Income Taxation of Corporations and Shareholders*, concerning one man organizations quoted by Mr. Thies, is as persuasive to me today as it was when I wrote it in 1959 (1st edition, p. 34); but I learned long ago not to confuse my theories with judicial judgments.

would be simple: let them copy the *Kintner* agreement. Whatever might have been the effect of such an agreement under the "earlier, largely overlooked jurisprudence" that Mr. Thies wishes to revive, however, its effect for at least half a century would almost certainly be to create a partnership under section 6(1) of the Uniform Partnership Act:

A partnership is an association of two or more persons to carry on as co-owners a business for profit.

A major characteristic of classic common law associations was a lack of capacity to own property, with the result that the members of such an association were co-owners of any property that was held in the group name. Contrary to Mr. Thies' suggestion at page 298, it is not the intent of the parties that determines whether an unincorporated association operated for profit is a partnership or not; its status under section 6(1) is involuntary, as businessmen seeking to avoid partnership status have often discovered to their dismay. Mr. Thies to the contrary notwithstanding, therefore, I continue to think that counsel for the taxpayer in the *Kintner* case was correct in conceding that the group was a partnership under local law; and that the same status would befall other groups using that agreement, in most if not all states.³ Once the agreement is brought within the aegis of the UPA, any contractual provisions conflicting with the statute (*e.g.*, attempts to create centralized management or continuity of life) must give way.

In view of the intended breadth of section 6(1) of the Uniform Partnership Act, it should not be surprising that the only classic common law associations that one now meets in real life—as distinguished from the pages of old law dictionaries—are voluntary, nonprofit clubs and similar groups. Indeed, the very legal encyclopedia on which Mr. Thies relies in support of his view that the *Kintner* group was a common law association rather than a partnership states:

[A]ccording to the rule generally recognized at the present time, the members of a voluntary association of individuals or of an unincorpo-

³I might add that if a business group did succeed in establishing itself as a non-partnership common law association, it would confront a morass of legal attributes that are either poorly suited, or positively antagonistic, to the conduct of business, including a lack of capacity to contract or sue in the group name. Although these and other disabilities are mitigated, to a degree that varies from state to state, by statutory provisions and judicial tolerance, they remain sufficiently troublesome even for nonprofit groups as to encourage them to organize under nonprofit membership corporation statutes. As a result, the law relating to common law associations has atrophied for want of exercise, and few businessmen or professional practitioners, if well-advised, would want to be governed by its rarely litigated vagaries. As I have argued in the text, however, they are protected against these uncharted seas by section 6(1) of the Uniform Partnership Act, which imposes partnership status willy-nilly on any such "association of two or more persons to carry on as co-owners a business for profit."

rated company organized for profit are to be considered as partners in their relations to third persons.⁴

Another encyclopedia is even more explicit:

Where . . . the association is organized for commercial purposes, and operated for pecuniary profit, it is no more than a partnership, and the rights and liabilities incident to that relation attach to its members, as well as between the members themselves, as between a member and the association, and as between members and third persons dealing with them or the association.⁵

For at least 50 years, then, the classic common law association has been the voluntary, nonprofit club or similar group; and one can hardly assume that *its* characteristics were the ones singled out by Congress as the only proper test of corporate tax liability for "associations" as that term is used in section 7701(a)(3).

It should not be an occasion for surprise, then, that the Supreme Court in *Hecht v. Malley* (relied on by Mr. Thies), eschewed his sweeping conclusion about the meaning of "association" in section 7701(a)(3), and instead held very cautiously:

We think that the word "association" as used in the [Revenue Act of 1918] clearly includes "Massachusetts Trusts" such as those herein involved, having quasi-corporate organizations under which they are engaged in carrying on business enterprises. What other form of "associations", if any, it includes, we need not, and do not, determine.⁶

The most that Mr. Thies has established, it seems to me, is that an unincorporated nonprofit group may be encompassed by the term "association" in section 7701(a)(3) if it possesses the characteristics of continuity of life and centralized management. If the common law association in question is operated for profit, however, it must first establish that it is not a partnership within the meaning of the local version of section 6(1) of the Uniform Partnership Act, since partnership status will render unenforceable any claim in its articles of association to continuity of life and centralized management. I see little or no possibility of surmounting this hurdle, even if the group follows the *Kintner* model with complete fidelity. For this reason, I cannot accept the central, and crucial, theorem of Mr. Thies' argument.

BORIS I. BITTKER

Southmayd Professor of Law, Yale Law School

⁴ 6 AM. JUR. 2d *Associations and Clubs* § 2 (1962) (footnote omitted).

⁵ 7 C.J.S. *Associations* § 1(3) (1937) (footnotes omitted).

⁶ 265 U.S. at 157 (footnote omitted).