STATE BOARD OF EQUALIZATION

October 27, 1969

Attention: X----------

Gentlemen:

Thank you for your illuminating brief of June 13, 1969, as to the "separateness" of X----------, a partnership consisting of X---------- and X----------, a joint venture of these same parties.

You point our that X---------- was formed on X---------- for the limited purpose of bidding and, if successful, constructing a subway "tube" X----------. On X---------- the construction was awarded X----------.

Approximately three months later on X----------, the parties who formed X----------, formed a general partnership, X----------. The partnership was formed specifically for the purpose of building and owning marine equipment which equipment was to be chartered to X---------- for use in the construct of X---------- tube. Each vessel was the subject of separate charter parties. When such equipment was not in use, it was occasionally chartered to other lessees. Most of the vessels have in fact been chartered to other persons.

You state that at all times the partners went to great lengths to maintain the separate identities of the parties in all of their respective dealings with creditors, customers, employees, X---------- and among the partners, themselves. Thus, the rental charged by one entity to the other was, in fact, an arms length fair rental. When it appeared that vendors dealing with both of the entities might be confused, a letter was sent to the vendors explaining the diversity. The partners in X-------- and the joint venturers in X---------- scheduled and held separate meetings.

You note that formation of separate entities resulted in substantial savings. Thus, while X-------- was required to pay workmen's compensation insurance premiums of $9.00 per each $100.00 of payroll, X---------'s premium was only $2.89 per each $100.00. Such savings resulted, in part, from the fact that all employees of X--------- were covered by the so-called "wrap-up" insurance required by the X----------,

whereas employees of X---------- were considered to be employees of a separate entity and, therefore, were not covered by the wrap-up insurance.

Further, the use of separate entities provided an "opportunity to insulate the construction and operation of marine equipment from labor difficulties. X---------- was subject to restrictive agreements with labor unions whereas X----------was not.

It should also be noted that there were several financial and accounting reasons for establishing X---------- and X---------- as separate entities. Thus, X---------- books and records were maintained, and the tax returns filed upon the so-called completed contract method of accounting, whereas X---------- books and records were maintained, and the tax and information returns filed upon the accrual method of accounting.

It is your contention that "As a matter of law, a joint venture and a general partnership are separate and distinct entities, not withstanding that each is composed of common members."

You point out that although partnership principles are applicable in part to joint ventures, there are several important distinctions. Thus while a corporation may participate in a
joint venture, it is generally barred from engaging in a partnership. 36 Virg. L.R. 444. This, historically, was California law. Milton Kaufman, Inc. v. Superior Court 210 P.2d 88 (1949). By weight of authority, in most jurisdictions a corporation may not enter into a partnership in the absence of statutory authorization.

Some courts have distinguished between a partnership and a joint venture on the grounds that there is no element of mutual agency in a joint venture. Generally, a partner is the agent of the other partners and can bind them in the ordinary course of business. Cal. Corp. Code, § 15009. On the other hand, the California "rule" is that a joint venturer does not have authority to bind the other joint venturers. Sime v. Malouf, 212 P.2d 946 (1950).

The "mutual agency" distinctions between partnerships and joint ventures become apparent in industry practices. Thus, the sponsoring joint venturer obtains a specific power of attorney from the other venturers authorizing him to perform specific limited acts. In fact, in the construction industry, the project owner frequently specifies the provisions to be contained in the power of attorney. By way of contrast, the powers of each of the partners in a partnership are set forth in substantial detail in the partnership agreement and, unless limited thereby, substantial powers of the various partners to bind each other are implied.

Similarly, although a new partner assumes the· then existing liability of the partnership, under California law, one does not impliedly assume obligations then existing even though such obligations were incurred in connection with the subject matter

of the joint venture. Enos v. Pacacho Gold Mining Co., 56 Cal. App. 765; 133 P.2d 633 (1943).

You further point out that the distinction between co-partnerships and joint ventures is recognized in the Sales and Use Tax Law itself. (§§ 6005, 6019.)

You also discuss the property and income tax aspects of the issue before us.

You state that both entities have consistently filed separate returns of tangible personal property with X---------- respectively, with the full knowledge of the respective assessors as to the nature of the entity. It was necessary for the entities to file separate petitions for review of such assessment and to file separate powers of attorney designating their respective representatives in both X----------. In fact, one of the entities almost failed to file a timely petition because its attorney-in-fact had inadvertently failed to sign the necessary document and the representative of the other entity was not allowed by the X---------- office to execute such document, even though it was doubtful whether the authorized individual would be able to execute the document before the deadline for filing had passed.

Recognition has been given by the Internal Revenue Service to the separate existence of three partnerships with identical general and limited partners. Where three partnerships with the same general partners and the same limited partners merged, the partnership contributing the greatest dollar value of assets is considered the resulting partnership and the other partnerships arc considered terminated. The partners in the terminated partnerships are considered to have received in liquidation partnership interests in the resulting partnership with a basis to them as determined under Code § 732(b). Rev. Rul. 68-289, 1968 I.R.B. 22.

Finally you observe that if this board adheres to its present position, the construction industry will suffer. The practice of joint venturing unusually large or hazardous projects is widespread. When major projects of the scope of the X---------- large dams are undertaken, only a handful of contractors can participate--even as participants in joint ventures. As a result, there is a fairly common phenomenon within the construction industry of multiple joint ventures, each consisting of identical members. If these joint ventures are not separate and distinct, there is an unanticipated risk that the resulting entity will be deemed an association taxable, for income tax purposes, as a corporation.

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We have reconsidered our position of November 20, 1968, in light of the arguments and points summarized above, and it is now our opinion that our initial position was erroneous and that under the factual situation as it exists in this case, X------ a joint venture, and X---------- a partnership, are separate persons for purposes of the sales tax law.

Whether we would regard other joint venture-partnership combinations, where the joint venture and the partnership are made up of identical members with identical interests in each "entity," as separate "persons" under section 6005 of the Revenue and Taxation Code would depend, as does our conclusion in this case, on the particular facts of the particular case.

Very truly yours,

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GJJ:ab
be: Out-of-State - District Administrator Chicago