

January 1952

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### Recommended Citation

Frank Moss, *Angels Must Pay Taxes or the Status of Theaters and Shows under the Internal Revenue Code*, 13 Mont. L. Rev. (1952).  
Available at: <http://scholarship.law.umt.edu/mlr/vol13/iss1/3>

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## Angels Must Pay Taxes or the Status of Theaters and Shows Under the Internal Revenue Code

\*FRANK MOSS

The recent case of *Junior Miss v. Commissioner*<sup>1</sup> raised some questions as to the tax consequences of producing a Broadway show. The immediate question before the tax court in that case was whether the form of enterprise producing the show *Junior Miss* resembled a corporation in enough respects to be taxed as an "association" under Section 3797 of the Internal Revenue Code?<sup>2</sup> However, the magic words "show business" put one's imagination into play and evoke numerous queries as to the tax treatment of other aspects of the production as well. For instance, how is the enterprise to be treated if it operates as a limited partnership? Can the producer who is also a general partner take a partnership deduction for the rent of his own theater? What about the actor or actress who invests in the enterprise as a limited partner but who also draws a salary? What is the tax treatment of the author who sells or leases his copyright to the business? What are the tax consequences resulting from a sale of an angel's interest?

The business enterprise which produces a Broadway show rarely, if ever, assumes the corporate form. In the main, this is because the producer does not wish to incur the double tax visited upon the dividend income of the corporate shareholder.<sup>3</sup> In the case of large corporate earnings (which would be the situation where a show is a "hit") the double taxation of dividend

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<sup>1</sup>14 Tax Court 1 (1950). Acquiesced C. B. 1950-1, 3.

<sup>2</sup>*Infra*, page 30.

<sup>3</sup>The corporation income tax applies to the entire net income of a corporation, and no deduction from gross income is allowed for amounts distributed as dividends to the shareholders. Any such dividends must be included in the personal returns of the shareholders, who receive no credit for the tax paid by the corporation. The result is that the portion of a corporation's income which is distributed as dividends is taxed twice.

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income becomes even more onerous.<sup>4</sup> One might add, if the corporation desires to accumulate the earnings to avoid the double tax there is still the possibility of the capital gains tax<sup>5</sup> upon sale of stock or liquidation, not to mention the danger of the Section 102 penalty surtax upon income accumulated beyond the reasonable needs of the business.<sup>6</sup>

On the other hand, a competing non-tax consideration is the desirability of a convenient method of financing a high cost production. Moderately wide sales of corporate stock with its advantages of limited liability and ready transferability can easily serve this purpose. Limited liability is especially attractive to the "angels," *i.e.* the financial backers of the show who will more readily risk investment if all they stand to lose upon failure of the enterprise is the original amount invested. However, the tax considerations militating against the use of the corporate form become overriding when there are in addition other modes of finance to take its place. Alternate forms of business enterprise, such as the joint venture utilized by producer Max Gordon in the *Junior Miss* case and the limited partnership which is in wide use today, nonetheless pose major tax problems.

If the producer wishes to save himself and the angels the double tax liability of incorporation but at the same time desires to utilize some corporate advantages such as limited liability without incorporating, will he nevertheless run the risk of having his business taxed as a corporation under Section 3797 of the I.R.C. and the Morrissey Doctrine?<sup>7</sup>

In the *Junior Miss* case the producer acquired non-assignable production rights in a play,<sup>8</sup> rented theaters, engaged actors,

<sup>4</sup>Under the 1950 Revenue Act corporations pay a 25% normal tax on all their taxable income and an additional 22% surtax on all taxable income over \$25,000 for the taxable year beginning after June 30, 1950, I.R.C. §§ 13, 15.

<sup>5</sup>I.R.C. § 117.

<sup>6</sup>I.R.C. § 102.

<sup>7</sup>*Morrissey v. CIR*, 296 U.S. 344, 56 S.Ct. 289, 80 L.Ed. 263 (1935).

<sup>8</sup>The producer enters into a contract with the author(s) called the "Minimum Basic Agreement" (of the Dramatists Guild, Authors' League of America and Theatrical Producing Managers) by which all production rights are "personal" between the author and the manager, and "neither the contract nor the rights granted thereby shall be assigned by the manager without the consent of the Guild except to a corporation in good standing with the Guild in which the assigning manager has control." Even then the manager is still personally liable on the contract, . . . "It being the intention of the parties hereto that rights herein conferred on the manager are personal to him and non-transferable and non-assignable by operation of law . . ." In 1945 the "Minimum Basic Agreement" was held invalid because in restraint of trade, *Ring v. Spina*, 148 Fed. 2d. 647, but is still in use today.

musicians, stage-hands, and bought costumes and scenery. To meet production costs he solicited and received from various acquaintances cash advances under separate contracts by which he agreed to repay the advance (after provision for a sinking fund of \$10,000) and to give the contributor a specified percentage of profits, if any; in case of loss the contributor agreed to forgive repayment of the advance and to bear an equal percentage of the loss. Management, control, and title to the property in the enterprise remained vested in the producer. The producer filed a partnership return under advice from his accountants. The commissioner assessed a deficiency on the ground that the enterprise was really an "association" under Section 3797(a) (3) of the Internal Revenue Code and hence was subject to corporate tax rates. The appropriate section is as follows:

Section 3797. Definitions:

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

(1) Person.—The term "person" shall be construed to mean and include an individual, a trust, estate, partnership, company, or corporation.

(2) Partnership and Partner.—The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

(3) Corporation. *The term "corporation" includes associations, joint-stock companies, and insurance companies. (Italics supplied).*

The tax court, in deciding for the taxpayer, held that the tests of corporateness as laid down in the regulations<sup>9</sup> and the *Morrissey* case<sup>10</sup> were not met. The regulations define an "association" subject to tax as a corporation as (1) any organization which continues notwithstanding changes in its participants, and (2) has a representative individual or board to conduct its affairs. In approving these characteristics as proper tests of *corporate resemblance*, the Supreme Court in *Morrissey v. CIR*<sup>11</sup> also stressed as significant (3) title to the property embarked in the enterprise

<sup>9</sup>Regulation 111, §§ 29.3797-1, 29.3797.2.

<sup>10</sup>*Supra*, note. 7.

<sup>11</sup>*Ibid.*

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held by a continuing body during the existence of the enterprise, (4) facility for the transfer of a participating interest in the enterprise, and (5) limitation of personal liability of the participants to property embarked in the undertaking.<sup>13</sup> Here, the tax court explained, even though the associates could transfer their interests, there was no continuing representative management nor was there limited liability. Title to the production rights, on which continuity of the venture depended were vested solely in the producer. The rights themselves were personal to him, and if he died the enterprise died with him. Likewise, his managerial position was not like that of a corporate officer or board of directors acting in a representative capacity for stockholders. The associates could not "grant or deny him managerial control since control was indefeasibly vested in him by contract with the authors."<sup>14</sup> That control would have lapsed by transfer of the production rights in violation of the contract or by the death of the producer.

The feature providing a percentage of profit and loss was not a limited liability device, the court stating at page 6:

"They acquired a right to a percent of the profits by guaranteeing to reimburse Gordon for a like percent of losses. This was no limited liability, as respondent suggests. If the play had been unsuccessful, they would have lost not only the advance, the only property risked by them in the enterprise, but their guaranteed part of the petitioner's losses, for which the contract fixed no bounds at all."

The Commissioner acquiesced<sup>14</sup> in the decision, but did not do so until after the Broadway producers agreed to operate all future productions as limited partnerships under New York law.<sup>15</sup>

Not long after the decision in the *Junior Miss* case was handed down the League of New York Theaters, Inc., representing most of the producers of New York City, secured an agreement<sup>16</sup> with the Bureau of Internal Revenue whereby the producers agreed to operate future productions as limited partner-

<sup>13</sup>The tests are not rigid, and the various features of ownership and administration must be considered as a whole for arriving at the classification of the entity. *CIR v. Brouillard*, 70 F. 2d. 154 (10th Cir. 1934); *Bert v. Helvering*, 67 App. D.C. 340, 92 F. 2d. 491 (1937).

<sup>14</sup>14 Tax Court 1, at page 8.

<sup>15</sup>*Supra*, note 1.

<sup>16</sup>The source is Mr. J. F. Reilly, Executive Director of the League of New York Theaters, Inc. The ruling is unpublished.

<sup>17</sup>*Ibid.*

ships under the New York Limited Partnership Law.<sup>17</sup> The regulations<sup>18</sup> state that a limited partnership is classified either as an ordinary partnership or an association taxable as a corporation depending on its characteristics in certain material respects. If the organization is not interrupted by the death of a general partner or by a change in the ownership of his participating interest, and if the management of its affairs is centralized in one or more persons acting in a representative capacity, it is taxable as a corporation.

The New York theater form of limited partnership enterprise consists of one or two general partners, the producers, who have active control and management of the business and a substantial share in the enterprise, and several limited partners who are contributing "angels." The limited partners have a percentage interest in the profits which is generally commensurate with their investment, but their liability is limited to the amount pledged as capital. They are subject to an "overall", that is, they are required to contribute more capital if the producer cannot meet the production requirements. But this is limited to their percentage interest, and there are no further obligations for additional contributions after production requirements are met. Limited partners' contributions are returnable only after the play opens in New York City and after payment or provision for all liabilities plus a cash reserve of X thousand dollars (anywhere from \$10,000 to \$25,000 is the usual amount depending on the size of the production). Substitution of limited partners is prohibited, and the partnership terminates on the death, insanity, or retirement of the general partners. This kind of enterprise clearly does not have the material corporate characteristics which would require it to be defined as an association subject to taxation as a corporation.<sup>19</sup> Although the management is centralized in the general partners they do not act merely in a representative capacity because they own a fairly substantial share of the partnership. Furthermore, they can neither be removed nor controlled by the limited partners because control is lodged in the general partners.<sup>20</sup> As to continuity of existence, the organization is interrupted by the death of the general partner or by a change in the ownership of his participating in-

<sup>17</sup>New York Partnership Law, Article 8. Montana has adopted the provisions of the Uniform Limited Partnership Act upon which the New York law is modeled. See § 63-701, et seq., R.C.M. 1947.

<sup>18</sup>Regulations, § 29.3797-5.

<sup>19</sup>Glensder Textile Co. v. CIR, 46 B.T.A. 176 (1942); Regulations, § 29:3797-5.

<sup>20</sup>Glensder Textile, *supra*, note 19.

terest because the partnership terminates on the death, insanity, or retirement of the general partners. The limited liability of the limited partners is not controlling because the persons who have active charge of the business are the general partners whose liability is unlimited.<sup>21</sup> As to transferability of interests, the limited partners are expressly prohibited by the partnership agreement from transferring their interests, and the general partner can not transfer his without ending the enterprise. Finally, the partnership does not hold property as an entity because under New York law the equitable right to the partnership property is in the several partners as tenants in partnership.<sup>22</sup>

It is important that the theater production stick to the foregoing limited partnership form in order that it may not be classified as a corporation.<sup>23</sup> Slight variations in form or operation may produce a substantial change in tax treatment. For example, if the general partners are without any substantial investment in the business and are acting as mere dummies and agents of the limited partners, then the commissioner would be justified in asserting a corporate tax. In *Glensder Textile Co. v. CIR*,<sup>24</sup> a decision holding a New York limited partnership non-taxable as a corporation, the Board of Tax Appeals posed the foregoing contention and implied that it would lead to a different tax result. The limited partners are in that case closely analogous to corporate shareholders, there being centralized representative management and limited liability of the interest holders.

Variations in state law likewise produce substantially different effects. Limited partnerships or partnership associations of the type authorized by the statutes of Pennsylvania, Michigan, and a few other states have consistently been held to be taxable as corporations by the regulations<sup>25</sup> and the courts.<sup>26</sup> Limited partnerships organized under the Uniform Limited Partnership Act, upon which the New York statute is modeled, however, have been held non-taxable as corporations by the courts,<sup>27</sup> even though the regulations make no distinction in regard to the latter.<sup>28</sup> The

<sup>21</sup>New York Partnership Law, § 98. For corresponding provision in Montana law see § 63-803, R.C.M. 1947.

<sup>22</sup>New York Partnership Law, § 51. For corresponding provision in Montana law see § 63-402, R.C.M. 1947.

<sup>23</sup>*Supra*, note 19.

<sup>24</sup>*Ibid.*

<sup>25</sup>Regulations, § 29.3797-6.

<sup>26</sup>*CIR v. Jacob Frost*, 13 T.C. 307 (1949); *Glensder Textile Co. v. CIR*, *Supra*, note 19.

<sup>27</sup>*Western Const. Co. v. CIR*, 14 T.C. 453 (1950); *aff'd* 191 F.2d (9th Cir. 1951); *Glensder Textile Co.*, *supra*, note 19. *Taywal Ltd. B.T.A. Memo. OP. Dkt. 107*, 115 July 20, 1942.

<sup>28</sup>Regulations, § 29.3797-5, last sentence.

difference is that the former, while nominally partnerships, provide for the limitation of liability of *all* the partners, whereas under the Uniform Limited Partnership Act only the limited partners have limited liability.

Montana has adopted substantially the provisions of the Uniform Limited Partnership Act,<sup>29</sup> and presumably a production organized under its provisions will not be held to be an association taxable as a corporation. In the recent case of *Western Construction Co. v. CIR.*<sup>30</sup> a limited partnership created under the limited partnership law of the State of Washington, which is modeled upon the Uniform Act, was held not to be an association taxable as a corporation on the authority of the *Glensder* case. It is thus safe to say that a production organized as a limited partnership under any state law which has adopted substantially the provisions of the Uniform Limited Partnership Act will not be held taxable as a corporation, provided, of course, that the enterprise does not resemble the dummy limited partnership hypothetically posed in the *Glensder* case.

However, the producers' worries do not end here. The use of the partnership form introduces other tax problems which are peculiar to that mode of conducting a business. These will be dealt with in the material following.

The Internal Revenue Code<sup>31</sup> does not provide a definite statutory concept of the nature of a partnership, sometimes treating it as an entity and sometimes treating it as a conduit through which the individual partners receive gain or loss. Thus, a partnership does not pay income tax as such, although it must file a partnership return.<sup>32</sup> It is an accounting entity for the purpose of computing the partnership net income<sup>33</sup> which is then taxed to the partners as individuals.<sup>34</sup> Each partner is made liable on his distributive share of such partnership income whether or not an actual distribution has been made.<sup>35</sup> He must include such share along with the rest of his taxable income in his individual return.<sup>36</sup> Likewise, each partner is entitled to his distributive share of any partnership losses.<sup>37</sup>

<sup>29</sup>R.C.M. 1947, § 63-701 et. seq.

<sup>30</sup>*Supra*, footnote 27.

<sup>31</sup>I.R.C. §§ 182-190.

<sup>32</sup>I.R.C. § 187.

<sup>33</sup>I.R.C. § 183.

<sup>34</sup>I.R.C. § 182.

<sup>35</sup>*Ibid.*

<sup>36</sup>Regulations, § 29.182-1.

<sup>37</sup>I.R.C. § 182.



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The computation of partnership net income follows the same rules as are applicable to the computation of the net income of any individual engaged in business, with a few specific statutory modifications.<sup>38</sup> Thus, the standard deduction, charitable contributions deduction, and net operating loss deduction are not allowed to the partnership, and adjustment therefor is made in the partners' returns.<sup>39</sup>

The following problems of partnership deductions, sale of a partner's interest, and the partner's basis lack comprehensive statutory coverage and are dealt with mostly on a decisional or administrative level. The problems are treated by the administrator and the courts as they arise, but there is no definite single principle emerging. Neither, it will be remembered, is there a definite statutory concept to be used as a guidepost. A description of the tax treatment and a partial analysis, however, can be attempted.

The producer who owns his own theater may list the rent paid to himself as a deductible expense of the partnership so long as it is a fixed charge and not a disguised distribution of profits. In the recent case of *Shirley v. O'Malley*<sup>40</sup> the district court so held on the basis of the above rationale as to rent on assets leased from the partners. It follows that if an author leased the production rights in his play to the partnership for a fixed charge and then also became a limited partner it would seem that his payments as "rent" could still be taken as a deductible expense. However, if payments are made in the form of royalties dependent on the profits of the enterprise it is implied that the commissioner would be upheld in asserting that they are a distribution of partnership earnings and not an expense, the court stating on page 100:

"It is true that the Butcher case is not squarely in point but the reasoning indicates that if the partnership is under a binding liability to one of the partners for the expense, that it should be allowed as a partnership deduction. . . . The collector in distinguishing the Butcher case from the case presently before us relies on the fact that there the rental payments were in no way tied up or contingent upon partnership profits. We can only point out that the rental payments were in no way tied up or contingent upon the partnership profits in this case."<sup>41</sup>

<sup>38</sup>I.R.C. § 183.

<sup>39</sup>I.R.C. §§ 183, 189.

<sup>40</sup>91 F. Supp. 98 (1950 D. Neb.)

<sup>41</sup>91 F. Supp. 98, at page 100.

Interest paid on the capital contributions of the partners is regarded as a distribution of profits or capital and not as an expense of the partnership.<sup>48</sup> A similar result obtains on payment for personal services of the partner. General Counsel's Memorandum 6582<sup>49</sup> states:

"The withdrawals of members of a partnership are not allowable deductions as salaries of such members in computing net income of the partnership for income tax purposes. . . . Partners are working for themselves and in contemplation of law a man may not constitute himself his own employee. . . . Therefore, whatever is received by a partner in the form of or under the name of salary constitutes nothing more or less than a withdrawal from the partnership of anticipated profits."

Thus, a producer may not deduct his salary for services as manager as an expense of the partnership. A more interesting problem is that of the "hit" performer who also owns a limited partnership interest. It is likely that the commissioner will not allow his or her salary to be taken as a deductible expense of the enterprise but will treat it as a distribution of earnings because in the eyes of the tax law "partners are working for themselves, and a man may not constitute himself his own employee."

Whether a particular item is a deductible expense of the partnership or is to be treated as a distribution of earnings to the individual partner usually should produce no difference in the immediate tax consequences. It is to be remembered that the partnership is an accounting entity and not a tax paying entity, and that the payments made to the partners are nevertheless taxable to them as their personal income even though the label may read "partnership expense." However, there may be instances where the difference is important. Consider, for example, a salary received in December, 1950, in the partner's calendar year 1950 but paid by a partnership whose fiscal year ends July 1, 1951. Because the salary is treated as a distribution of profits it has taxable consequences for the partner in 1951 and not 1950. This is so because a partner is taxable on his distributive share of the partnership income for its taxable year ending within the partner's taxable year.<sup>48</sup> If the salary were treated as a partnership expense and not as a distribution of profits, pre-

<sup>48</sup>I.T. 2503, VIII-2 C.B. 145 (1929) ; CIR v. Banfield, 122 F. 2d. 1017 (9th Cir. 1941) ; Regulations, § 29.183-1, last sentence.

<sup>49</sup>VIII-2 C.B. 200 (1929).

<sup>50</sup>I.R.C. § 188.

sumably he would have to include it in his 1950 income, and the partnership would take the deduction in 1951.<sup>45</sup>

The sale of a partner's interest stimulates certain problems. A recent news item mentioned that the investors (limited partners) in "Guys and Dolls" were offered a 400% profit by a syndicate if they would sell their interests in that "hit" production.<sup>46</sup> Assuming buyer and seller can get together on the price and assuming no objection is raised by the other members of the partnership agreement (substitution of limited partners is generally prohibited), what is the tax treatment of the selling partner?

Formerly, it was the position of the commissioner that the sale of a partnership interest was a sale of the selling partner's undivided interest in each specific partnership asset. Today, however, he has changed his position in the face of overwhelming authority to the contrary and now treats the sale of a partnership interest as the sale of a capital asset under Section 117 of the Internal Revenue Code.<sup>47</sup> Hence, considerable tax savings can be effected by a limited partner who sells his interest in a successful show. In effect he is selling his right to future profits which will now be taxed at capital gain rates rather than ordinary rates.<sup>48</sup> However, the valuation of a future interest in the profits of an enterprise of such indefinite and variable duration as a Broadway show is a practical consideration that must be reckoned with when buyer and seller get together.

The method of distributing the cash proceeds was described above. After all liabilities are met and a fixed reserve for contingent losses is set up, a return of the limited partner's contribution is then made before profits are distributed. The reserve, if not exhausted, is distributed on dissolution. This method of distribution raises some problems as to the adjustments to be made in the individual partner's basis.

The partner's basis is originally the amount that he contributes to the enterprise.<sup>49</sup> Thereafter, it is adjusted up or down to reflect certain aspects of partnership activity. Thus, if the partner did not draw off his distributive share of the partnership profits for the year he is nevertheless taxable on such share and

<sup>45</sup>*Cf.* Shirley v. O'Malley, *supra*, note 40, where rent on assets received by the partner in 1942 was income to the partner in 1942 and a deduction to the partnership in 1943.

<sup>46</sup>Leonard Lyon's Column, New York Post, Nov. 30, 1950.

<sup>47</sup>G.C.M. 26379, C.B. 1950-1, 58 (1950).

<sup>48</sup>I.R.C. § 117.

<sup>49</sup>I.R.C. § 113(a).

the amount is added to the basis of his partnership interest.<sup>60</sup> In this context the cash reserve set aside out of partnership profits for the year would fall into the category of undistributed partnership earnings; each partner would be taxable on his distributive share, and his basis would accordingly be increased. Furthermore, cash distributions representing a return of the partner's contributions produce no tax because they are a return of capital, but the basis of the partner's interest is accordingly reduced. If an operating loss occurs the partner may use his share of such loss as a deduction against his other income, and he also decreases the basis of his partnership interest by the amount of the loss.<sup>61</sup> Upon dissolution, where the usual method is to distribute any remaining cash proportionately, it is evident that normally no gain or loss should be recognized. The intermediate adjustments which the partner has made in his basis will equalize the basis and the amount distributed. However, this equality may not exist where the partner is one who has bought his interest from a prior partner. Here, gain may result when the cash distribution exceeds the basis, and loss where on dissolution it is less than the basis.

The Revenue Act of 1950 excludes "a copyright, literary, musical or artistic composition, or similar property" from the definition as a *capital asset* under Section 117 (a) (1) of the Internal Revenue Code. This is true whether the foregoing property is in the creator's hands or is in the hands of one to whom he has made a gift of the property.<sup>62</sup> The Act thus eliminates any doubts existing before its passage that the income received by an author for his work is to be taxed as ordinary income. Prior to the Act there was a distinction drawn between a professional writer or other creator of artistic works and the amateur who produced an occasional original creation. The professional was taxed at ordinary rates (whether he received royalties or sold the product outright) because the products of his work were held "primarily for sale to customers in the ordinary course of his trade or business."<sup>63</sup> The amateur received capital gain treatment on the sale of his creative works.<sup>64</sup> The 1950 Act eliminates this distinction but is applicable to taxable years beginning after September 23, 1950, the date of enactment.

The Section 107(b)<sup>65</sup> spread-provision still remains in the

<sup>60</sup>Regulations, § 29.113(a) 13-2.

<sup>61</sup>Appeal of Meyer, 3 B.T.A. 329 (1926).

<sup>62</sup>I.R.C. § 117(a) (1) (c) ii.

<sup>63</sup>Goldsmith v. CIR, 143 F. 2d. 466 (2nd Cir. 1944).

<sup>64</sup>Dreyman v. CIR, 11 T.C. 153 (1948); cf. "Eisenhower Book Sale," N.Y. Herald-Tribune Oct. 3, 1948.

<sup>65</sup>I.R.C. § 107(b).

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law allowing the income from an artistic work to be "spread" over the time (not exceeding 36 months) the work was done (a) if the time spent from commencement to completion is at least 36 months and (b) if at least 80% of the total gross income from the work is received only within the taxable year. The author who sells his copyright outright and receives all the cash he is ever going to get for it within the taxable year may clearly get the benefit of the above provision if he complies with the 36 month work-requirement. However, the author of a "hit" who leases production rights in the play to the producer in return for royalties running as long as the show runs will not likely be able to take advantage of the provision even if he complies with the 36 month work-period. A good "hit" may run well over a year, not to mention the fact that the author may later receive further gains by the sale of the radio, television, and movie rights. Thus, it is seen that the Section 107 (b) provision is restricted in its scope and is not likely to be of help to the playwright of a very successful production.

Producers of "hit" shows which have heavy advance ticket sales running into future tax years should be aware of the tax consequences. It is generally held that payments received for the performance of future services are income at the time of receipt and may not be deferred until the taxable year when performance is to be made.<sup>66</sup> Likewise, if the taxpayer seeks to nullify the receipt of the income by setting up a reserve for anticipated liabilities and taking it as a deduction he will be defeated by the commissioner.<sup>67</sup> Thus, even though a manager may be obligated to make a refund to the customers if the show cannot go on at a future date, the money received for advance ticket sales is nevertheless taxable income at the time of receipt.<sup>68</sup>

Such items as scenery and costumes, which are an ever-present financial headache to the producer, may be the subject of a depreciation allowance. The Regulations, Section 29.23(e)-2, last sentence, state:

"Properties and costumes used exclusively in a business, such as a theatrical business, may be the subject of a depreciation allowance."

<sup>66</sup>Your Health Club, 4 T.C. 385 (1944); South Dade Farms, Inc. v. CIR, 138 F. 2d. 818 (5th Cir. 1943); South Tacoma Motor Co., 3 T.C. 411 (1949); National Airlines, Inc., 9 T.C. 159 (1947); Capital Warehouse Co. Inc., 9 T.C. 966 (1947); aff'd 171 F. 2d. 395 (8th Cir. 1948). *Contra*: Vienstra & De Haen Coal Co., 11 T.C. 964 (1948).

<sup>67</sup>Brown v. Helvering, 291 U.S. 193 (1934).

<sup>68</sup>National Airlines Inc.; Your Health Club, *supra*, note 56.

In conclusion it may be stated that the use of the New York limited partnership as a business device to finance a Broadway show solves the major problem of the producer and the "angel," both of whom wish to avoid the double taxation of corporate shareholder income and yet retain limited liability for the latter. Limited partnerships organized under the Uniform Limited Partnership Act, upon which the New York statute is modeled, do not conform to the five salient features of corporate resemblance which would make them "associations" taxable as corporations under the Morrissey Doctrine, but variations according to differing state laws or manipulations in form and operations may lead to a different tax result.

However, operation of a theater production as a limited partnership opens up further tax problems which are peculiar to the partnership form of doing business, and each problem must be dealt with on an individual basis. Sometimes the conduit approach is adopted, and at other times the entity approach is used leading to workable but differing results. Thus, (a) payments in the form of salaries, royalties, or interest to the partners are regarded as distributions of partnership earnings and not as deductible expenses of the partnership (conduit), whereas payment as rent for the theater to a partner may be a partnership expense (entity); (b) the sale of a limited partner's interest is now treated by the Bureau as the sale of a capital asset (entity), whereas it was formerly treated as the sale of an interest in each individual asset (conduit); (c) the partner's basis, which is the amount originally contributed to the enterprise, is intermediately adjusted to reflect undistributed partnership earnings or partnership losses and consequently no gain or loss is realized where cash only is distributed to the partners on dissolution (conduit). A new statutory approach may well be needed to dispel the seeming confusion.