2022

Instructions for Form 1065

U.S. Return of Partnership Income

Volume 3 of 6

Department of the Treasury
Internal Revenue Service

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Do not report portfolio or rental activity income (loss) on this line.

Deductions

Report only trade or business activity deductions on lines 9 through 20. Do not report the following expenses on lines 9 through 20.

- Rental activity expenses. Report these expenses on Form 8825 or line 3b of Schedule K.
- Deductions allocable to portfolio income. Report these deductions on line 13d of Schedule K and in box 13 of Schedule K-1 using code I or L.
- Nondeductible expenses (for example, expenses connected with the production of tax-exempt income). Report nondeductible expenses on line 18c of Schedule K and in box 18 of Schedule K-1 using code C.

- Qualified expenditures to which an election under section 59(e) may apply. The instructions for line 13c of Schedule K and for Schedule K-1, box 13, code J, explain how to report these amounts.
- Items the partnership must state separately that require separate computations by the partners. Examples include expenses incurred for the production of income instead of in a trade or business, charitable contributions, foreign taxes paid or accrued, intangible drilling and development costs, soil and water conservation expenditures, amortizable basis of reforestation expenditures, and exploration expenditures. The distributive shares of these expenses are reported separately to each partner on Schedule K-1.

Limitations on Deductions

Section 263A uniform capitalization rules. The uniform capitalization rules of section 263A generally require partnerships to capitalize certain costs incurred in connection with the following.

- The production of real property and tangible personal property held in inventory or held for sale in the ordinary course of business.
- Real property or personal property (tangible and intangible) acquired for resale.
- The production of real property and tangible personal property by a partnership for use in its trade or business or in an activity engaged in for profit.

Tangible personal property produced by a partnership includes a film, sound recording, videotape, book, or similar property.

The costs required to be capitalized under section 263A aren't deductible until the property to which the costs relate is sold, used, or otherwise disposed of by the partnership.

Exceptions. For tax years beginning after 2017, a small business taxpayer, defined earlier, can adopt or change its method of accounting to not capitalize costs under section 263A. See section 263A(i) and *Accounting Methods*, earlier. Section 263A doesn't apply to the following.

- Timber.
- Most property produced under a long-term contract.
- Certain property produced in a farming business. See the note at the end of the instructions for line 5, earlier.
- Geological and geophysical costs amortized under section 167(h).

- Certain plants bearing fruits and nuts under section 168(k)(5).

The partnership must report the following costs separately to the partners for purposes of determinations under section 59(e).

- Research and experimental costs under section 174.
- Intangible drilling costs for oil, gas, and geothermal property.
- Mining exploration and development costs.

Indirect costs. Partnerships subject to the uniform capitalization rules are required to capitalize not only direct costs but an allocable part of most indirect costs (including taxes) that benefit the assets produced or acquired for resale, or are incurred because of the performance of production or resale activities.

For inventory, indirect costs that must be capitalized include the following.

- Administration expenses.
- Taxes.
- Depreciation.
- Insurance.
- Compensation paid to officers attributable to services.
- Rework labor.
- Contributions to pension, stock bonus, and certain profit-sharing, annuity, or deferred compensation plans.

Regulations section 1.263A-1(e)(3) specifies other indirect costs that relate to production or resale activities that must be capitalized and those that may be currently deductible.

Interest expense paid or incurred during the production period of designated property must be capitalized and is governed by

special rules. For more details, see Regulations sections 1.263A-8 through 1.263A-15.

For more details on the uniform capitalization rules, see Regulations sections 1.263A-1 through 1.263A-3.

Transactions between related taxpayers. Generally, an accrual basis partnership can deduct business expenses and interest owed to a related party (including any partner) only in the tax year of the partnership that includes the day on which the payment is includible in the income of the related party. See section 267 for details.

Business interest. Business interest expense is limited for tax years beginning after 2017. See section 163(j) for limitations on deductions for business interest, and section 163(j)(4) for rules specific to partnerships.

Business startup and organizational costs. Generally, a partnership can elect to deduct a limited amount of startup or organizational costs paid or incurred. Any costs not deducted must be amortized as explained below. See sections 195(b) and 709(b).

Time for making an election. The partnership generally elects to deduct startup or organizational costs by claiming the deduction on its return filed by the due date (including extensions) for the tax year in which the active trade or business begins. However, for startup or organizational costs paid or incurred before September 9, 2008, the partnership may be required to attach a statement to its return to elect to deduct such costs. See Temporary Regulations sections 1.195-1T and 1.709-1T (as in effect on July 7, 2008) for details. Also, see Regulations sections 1.195-1 and 1.709-1. If the partnership timely filed its return for the year

without making an election, it can still make an election by filing an amended return within 6 months of the due date of the return (excluding extensions). Clearly indicate the election on the amended return and enter "Filed pursuant to section 301.9100-2" at the top of the amended return. File the amended return at the same address the partnership filed its original return. The election applies when figuring income for the current tax year and all subsequent years.

The partnership can choose to forgo the above elections by clearly electing to capitalize its startup or organizational costs on its return filed by the due date (including extensions) for the tax year in which the active trade or business begins.

The election to either amortize or capitalize startup or organizational costs is irrevocable and applies to all startup and organizational costs that are related to the trade or business.

Amortization. Any costs not deducted under the above rules must be amortized ratably over a 180-month period, beginning with the month the partnership begins business. See the Instructions for Form 4562 for details.

Report the deductible amount of these costs and any amortization on line 20. For amortization that began during the tax year, complete and attach Form 4562, Depreciation and Amortization.

Syndication costs. Costs for issuing and marketing interests in the partnership, such as commissions, professional fees, and printing costs, must be capitalized. They cannot be depreciated or amortized. See the instructions for line 10, later, for the treatment of syndication fees paid to a partner.

Reducing certain expenses for which credits are allowable. The partnership may need to reduce the otherwise allowable deductions for expenses used to figure certain

credits. The following are examples of such credits. (Do not reduce the amount of the allowable deduction for any portion of the credit that was passed through to the partnership from another pass-through entity.)

1. Work opportunity credit.
2. Credit for increasing research activities.
3. Disabled access credit.
4. Empowerment zone employment credit, if applicable.
5. Indian employment credit, if applicable.
6. Credit for employer social security and Medicare taxes paid on certain employee tips.
7. Orphan drug credit.
8. Credit for small employer pension plan startup costs and auto-enrollment.
9. Credit for employer-provided childcare facilities and services.

10. Low sulfur diesel fuel production credit.
11. Mine rescue team training credit, if applicable.
12. Credit for employer differential wage payments.
13. Credit for small employer health insurance premiums.
14. Employer credit for paid family and medical leave (Form 8994).
15. Employee retention credit for employers affected by qualified disasters (Form 5884-A).

Note. Wages taken into account in determining the credit for qualified sick and family leave on Form 941 cannot be taken into account in determining the employer credit for paid family and medical leave on Form 8994. See the Instructions for Form 8994.

If the partnership has any of the credits listed above, figure each current year credit before figuring the deductions for expenses on which the credit is based.

Line 9. Salaries and Wages

Enter the salaries and wages paid or incurred for the tax year, reduced by the amount of the following credit(s).

- Work Opportunity Credit (Form 5884).
- Empowerment Zone Employment Credit (Form 8844), if applicable.
- Indian Employment Credit (Form 8845), if applicable.
- Mine Rescue Team Training Credit (Form 8923), if applicable.
- Credit for Employer Differential Wage Payments (Form 8932).

- Employee Retention Credit for Employers Affected by Qualified Disasters (Form 5884-A).

Do not reduce the amount of the allowable deduction for any portion of the credit that was passed through to the partnership from another pass-through entity. See the instructions for the credit form for more information.

Do not include salaries and wages reported elsewhere on the return, such as amounts included in cost of goods sold, elective contributions to a section 401(k) cash or deferred arrangement, or amounts contributed under a salary reduction SEP agreement or a SIMPLE IRA plan.

Line 10. Guaranteed Payments to Partners

Deduct payments or credits to a partner for services or for the use of capital if the payments or credits are determined without

regard to partnership income and are allocable to a trade or business activity. Also include on line 10 amounts paid during the tax year for insurance that constitutes medical care for a partner, a partner's spouse, a partner's dependents, or a partner's children under age 27 who aren't dependents.

For information on how to treat the partnership's contribution to a partner's health savings account (HSA), see Notice 2005-8, 2005-4 I.R.B. 368.

Do not include any payments and credits that should be capitalized. For example, although payments or credits to a partner for services rendered in syndicating a partnership may be guaranteed payments, they aren't deductible on line 10. They are capital expenditures. However, they should be reported as guaranteed payments on the applicable line of Schedule K, line 4b, and in box 4b of Schedule K-1.

Do not include distributive shares of partnership profits.

Report the guaranteed payments to the appropriate partners using the applicable box 4 of Schedule K-1.

Line 11. Repairs and Maintenance

Enter the cost of repairs and maintenance not claimed elsewhere on the return, such as labor and supplies, that are not payments for improvements to the partnership's property. Amounts are paid for improvements if they are for betterments to the property, for restorations of the property (such as the replacements of major components or substantial structural parts), or if they adapt the property to a new or different use. Improvements must be capitalized. See Regulations section 1.263(a)-3.

The partnership can deduct repair and maintenance expenses only to the extent they relate to a trade or business activity. See

Regulations section 1.162-4. The partnership may elect to capitalize certain repair and maintenance costs consistent with its books and records. See Regulations section 1.263(a)-3(n) for information on how to make the election.

Line 12. Bad Debts

Enter the total debts that became worthless in whole or in part during the year, but only to the extent such debts relate to a trade or business activity. Report deductible nonbusiness bad debts as a short-term capital loss on Form 8949.

Cash method partnerships cannot take a bad debt deduction unless the amount was previously included in income.

Line 13. Rent

Enter rent paid on business property used in a trade or business activity. Do not deduct rent

for a dwelling unit occupied by any partner for personal use.

If the partnership rented or leased a vehicle, enter the total annual rent or lease expense paid or incurred in the trade or business activities of the partnership. Also complete Part V of Form 4562. If the partnership leased a vehicle for a term of 30 days or more, the deduction for vehicle lease expense may have to be reduced by an amount called the inclusion amount. The partnership may have an inclusion amount if:

The lease term began:	**And the vehicle's FMV on the first day of the lease exceeded:**
Automobiles other than trucks and vans	
During calendar year 2022.....	$56,000

During calendar year 2021.....	$51,000
After 12/31/2017 but before 1/1/2021.....	$50,000
After 12/31/12 and before 1/1/18.....	$19,000
After 12/31/09 but before 1/1/13.....	$18,500

Trucks and vans

During calendar year 2022.....	$56,000
During calendar year 2021.....	$51,000
After 12/31/2017 but before 1/1/2021.....	$50,000
After 12/31/13 and before 1/1/18.....	$19,500

After 12/31/09 and before 1/1/14.....	$19,000

The inclusion amount for lease terms beginning in 2023 will be published in the Internal Revenue Bulletin in early 2023.

See Pub. 463, Travel, Gift, and Car Expenses, for instructions on figuring the inclusion amount.

Line 14. Taxes and Licenses

Enter taxes and licenses paid or incurred in the trade or business activities of the partnership if not reflected elsewhere on the return. Federal import duties and federal excise and stamp taxes are deductible only if paid or incurred in carrying on the trade or business of the partnership. Foreign taxes are included on line 14 only if they are deductible and not creditable taxes under sections 901 and 903. See Schedule K-2, Part II, Section

2, line 45, column (g). Do not deduct the following taxes on line 14.

- Taxes not imposed on the partnership.
- Federal income taxes or taxes reported elsewhere on the return.
- Creditable foreign taxes under sections 901 and 903. Report these taxes separately on Schedule K, line 21, and in box 21 of Schedule K-1.
- Taxes allocable to a rental activity. Report taxes allocable to rental real estate activity on Form 8825. Report taxes allocable to a rental activity other than a rental real estate activity on line 3b of Schedule K.
- Taxes paid or incurred for the production or collection of income, or for the management, conservation, or maintenance of property held to produce income. Report these taxes separately on line 13d of Schedule K

and in box 13 of Schedule K-1 using code W.See section 263A(a) for rules on capitalization of allocable costs (including taxes) for any property.

- Taxes, including state or local sales taxes, that are paid or incurred in connection with an acquisition or disposition of property (these taxes must be treated as a part of the cost of the acquired property or, in the case of a disposition, as a reduction in the amount realized on the disposition).
- Taxes assessed against local benefits that increase the value of the property assessed (such as for paving, etc.).

See section 164(d) for information on apportionment of taxes on real property between seller and purchaser.

Do not reduce your deduction for social security and **!** *Medicare taxes by the nonrefundable and refundable portions*

of the FFCRA and ARP credits for qualified sick and family leave wages claimed on the partnership's employment tax returns. Instead, report the credits as income on line 7.

Line 15. Interest

Include only interest incurred in the trade or business activities of the partnership that isn't claimed elsewhere on the return. Do not include interest expense on the following.

- Debt used to purchase rental property or debt used in a rental activity. Interest allocable to a rental real estate activity is reported on Form 8825 and is used in arriving at net income (loss) from rental real estate activities on line 2 of Schedule K and in box 2 of Schedule K-1. Interest allocable to a rental activity other than a rental real estate activity is included on line 3b of Schedule K and is used in

arriving at net income (loss) from a rental activity (other than a rental real estate activity). This net amount is reported on line 3c of Schedule K and in box 3 of Schedule K-1.

- Debt used to buy property held for investment. Interest that is clearly and directly allocable to interest, dividend, royalty, or annuity income not derived in the ordinary course of a trade or business is reported on line 13b of Schedule K and in box 13 of Schedule K-1 using code H. See the instructions for line 13b of Schedule K; box 13, code H, of Schedule K-1; and Form 4952, Investment Interest Expense Deduction, for more information on investment property.
- Debt proceeds allocated to distributions made to partners during the tax year. Instead, report such interest on line 13d of Schedule K and

in box 13 of Schedule K-1 using code W. To determine the amount to allocate to distributions to partners, see Notice 89-35, 1989-1 C.B. 675.

- Debt required to be allocated to the production of designated property. Designated property includes real property, personal property that has a class life of 20 years or more, and other tangible property requiring more than 2 years (1 year in the case of property with a cost of more than $1 million) to produce or construct. Interest allocable to designated property produced by a partnership for its own use or for sale must be capitalized. In addition, a partnership must also capitalize to the basis of the designated property any interest on debt allocable to an asset used to produce designated property. A partner may have to capitalize interest

that the partner incurs during the tax year for the partnership's production expenditures. Similarly, interest incurred by a partnership may have to be capitalized by a partner for the partner's own production expenditures. The information required by the partner to properly capitalize interest for this purpose must be provided by the partnership on an attached statement for box 20 of Schedule K-1 using code R. See section 263A(f) and Regulations sections 1.263A-8 through 1.263A-15.

Special rules apply to the following.

- Allocating interest expense among activities so that the limitations on passive activity losses, investment interest, and personal interest can be properly figured. Generally, interest expense is allocated in the same manner as debt is allocated. Debt is

allocated by tracing disbursements of the debt proceeds to specific expenditures. Temporary Regulations section 1.163-8T gives rules for tracing debt proceeds to expenditures. Also see Proposed Regulations 1.163-14 for a special rule for allocating interest expense with respect to pass-through entities.

- Interest paid by a partnership to a partner for the use of capital, which should be entered on line 10 as guaranteed payments.
- Prepaid interest, which can generally only be deducted over the term of the debt. See section 461(g) and Regulations sections 1.163-7, 1.446-2, and 1.1273-2(g) for details.
- Interest that is allocable to unborrowed policy cash values of life insurance, endowment, or annuity contracts issued after June 8, 1997,

when the partnership is a policyholder or beneficiary. See section 264(f). Attach a statement showing the computation of the deduction.

Limitation on deduction. Business interest expense deduction is generally limited to the sum of business interest income, 30% of the adjusted taxable income (ATI), and floor plan financing interest. This limitation generally applies at the partnership level. See section 163(j)(4) for additional information about the application of the business interest expense limitation to partnerships. See Form 8990, Limitation on Business Interest Expense Under Section 163(j), and its instructions for more information. Business interest expense includes any interest expense properly allocable to a trade or business. A small business taxpayer that isn't a tax shelter (as defined in section 448(d)(3)) and that meets the gross receipts test isn't required to limit business interest expense under section

163(j). A taxpayer meets the gross receipts test if the taxpayer has average annual gross receipts of $27 million or less for the 3 prior tax years under the gross receipts test of section 448(c). Gross receipts include the aggregate gross receipts from all persons treated as a single employer such as a controlled group of corporations, commonly controlled partnerships or proprietorships, and affiliated service groups. If the partnership fails to meet the gross receipts test, Form 8990 is generally required. Also see Schedule B, questions 23 and 24.

Line 16. Depreciation

On line 16a, enter only the depreciation claimed on assets used in a trade or business activity. Enter on line 16b the depreciation included elsewhere on the return (for example, on page 1, line 2) that is attributable to assets used in trade or business activities. See the Instructions for Form 4562, or Pub. 946, How To Depreciate

Property, to figure the amount of depreciation to enter on this line.

Complete and attach Form 4562 only if the partnership placed property in service during the tax year or claims depreciation on any car or other listed property.

Do not include any section 179 expense deduction on this line. This amount isn't deducted by the partnership. Instead, it is passed through to the partners in box 12 of Schedule K-1. Generally, the basis of a partnership's section 179 property must be reduced to reflect the amount of section 179 expense elected by the partnership. This reduction must be made in the basis of partnership property even if the limitations of section 179(b) and Regulations section 1.179-2 prevent a partner from deducting all or a portion of the amount of the section 179 expense allocated by the partnership.

Line 17. Depletion

If the partnership claims a deduction for timber depletion, complete and attach Form T (Timber), Forest Activities Schedule.

Do not deduct depletion for oil and gas properties. Each partner figures depletion on oil and gas properties. See the instructions for Schedule K-1, box 20, Depletion information oil and gas (code T)*, for the information on oil and gas depletion that must be supplied to the partners by the partnership.*

Line 18. Retirement Plans, etc.

Do not deduct payments for partners to retirement or deferred compensation plans including IRAs, qualified plans, and simplified employee pension (SEP) and SIMPLE IRA plans on this line. These amounts are reported in box 13 of Schedule K-1, using code R, and are deducted by the partners on their own returns.

Enter the deductible contributions not claimed elsewhere on the return made by the partnership for its common-law employees under a qualified pension, profit-sharing, annuity, or SEP or SIMPLE IRA plan, and under any other deferred compensation plan.

If the partnership contributes to an IRA for employees, include the contribution in salaries and wages on page 1, line 9, or Form 1125-A, line 3, and not on line 18.

Employers who maintain a pension, profit-sharing, or other funded deferred compensation plan (other than a SEP or SIMPLE IRA), whether or not the plan is qualified under the Internal Revenue Code and whether or not a deduction is claimed for the current year, must generally file the applicable form listed below.

- Form 5500, Annual Return/Report of Employee Benefit Plan.

- Form 5500-SF, Short Form Annual Return/Report of Small Employee Benefit Plan (generally filed instead of Form 5500 if there are under 100 participants at the beginning of the plan year).

Form 5500 and Form 5500-SF must be filed electronically under the computerized ERISA Filing Acceptance System (EFAST2). For more information, see the EFAST2 website at EFAST.dol.gov.

- Form 5500-EZ, Annual Return of A One-Participant (Owners/ Partners and Their Spouses) Retirement Plan or A Foreign Plan. File this form for a plan that only covers one or more partners (or partners and their spouses) or a foreign plan that is required to file an annual return and does not file the annual return electronically on Form 5500-SF.

Line 19. Employee Benefit Programs

Enter the partnership's contributions to employee benefit programs not claimed elsewhere on the return (for example, insurance, health, and welfare programs) that aren't part of a pension, profit-sharing, etc., plan included on line 18.

Do not include amounts paid during the tax year for insurance that constitutes medical care for a partner, a partner's spouse, a partner's dependents, or a partner's children under age 27 who aren't dependents. Instead, include these amounts on line 10 as guaranteed payments on the applicable line of Schedule K, line 4, and the applicable line of box 4 of Schedule K-1, of each partner on whose behalf the amounts were paid. Also report these amounts on Schedule K, line 13d, and in box 13 of Schedule K-1, using code M, of each partner on whose behalf the amounts were paid.

Line 20. Other Deductions

Enter the total allowable trade or business deductions that aren't deductible elsewhere on page 1 of Form 1065. Attach a statement listing by type and amount each deduction included on this line. Examples of other deductions include the following.

- Amortization. See the Instructions for Form 4562 for more information. Complete and attach Form 4562 if the partnership is claiming amortization of costs that began during the tax year.
- Insurance premiums.
- Legal and professional fees.
- Supplies used and consumed in the business.
- Utilities.
- Certain business startup and organizational costs. See *Limitations*

on Deductions, earlier, for more details.

- Deduction for certain energy efficient commercial building property. See section 179D; and Notice 2006-52, 2006-26 I.R.B. 1175, as amplified and clarified by Notice 2008-40, 2008-14 I.R.B. 725, and modified by Notice 2012-26, 2012-17 I.R.B. 847. Attach Form 7205, Energy Efficient Commercial Building Deduction.
- Any net negative section 481(a) adjustment.

Also see *Special Rules*, later.

Do not deduct the following on line 20.

- Items that must be reported separately on Schedules K and K-1.
- Fines or similar penalties. Generally, no deduction is allowed for fines or similar penalties paid to or at the

direction of a government or governmental entity for violating any law except amounts that constitute restitution (including remediation of property), amounts paid to come into compliance with the law, amounts paid or incurred as the result of orders or agreements in which no government or governmental entity is a party, and amounts paid or incurred for taxes due to the extent the amount would have been allowed as a deduction if timely paid. No deduction is allowed unless the amounts are specifically identified in the order or agreement and the taxpayer establishes that the amounts were paid for that purpose. Also, any amount paid or incurred as reimbursement to the government for the costs of any investigation or litigation are not eligible for the exceptions and are nondeductible. See

section 162(f). Report nondeductible amounts on Schedule K, line 18c.

- Expenses allocable to tax-exempt income. Report these expenses on Schedule K, line 18c.

- Net operating losses. Only individuals and corporations may claim a net operating loss deduction.

- Amounts paid or incurred to participate or intervene in any political campaign on behalf of a candidate for public office, or to influence the general public regarding legislative matters, elections, or referendums. Report these expenses on Schedule K, line 18c.

- Lobbying expenses. Generally, lobbying expenses are not deductible. These expenses include amounts paid or incurred in connection with influencing federal, state, or local

legislation; or amounts paid or incurred in connection with any communication with certain federal executive branch officials in an attempt to influence the official actions or positions of the officials. See Regulations section 1.162-29 for the definition of “influencing legislation.” Dues and other similar amounts paid to certain tax-exempt organizations may not be deductible. If certain in-house lobbying expenditures don't exceed $2,000, they are deductible. See section 162(e)(4)(B).

- Amounts paid or incurred for any settlement or payout related to sexual harassment or sexual abuse that is subject to a nondisclosure agreement, as well as any attorney’s fees related to the settlement or payout. See section 162(q).

Special Rules

Travel, meals, and entertainment. Subject to limitations and restrictions discussed below, a partnership can deduct ordinary and necessary travel and non-entertainment-related meal expenses paid or incurred in its trade or business. Generally, entertainment expenses, membership dues, and facilities used in connection with these activities cannot be deducted. Also, special rules apply to deductions for gifts, luxury water travel, and convention expenses. See section 274 and Pub. 463 for details.

Travel. The partnership cannot deduct travel expenses of any individual accompanying a partner or partnership employee, including a spouse or dependent of the partner or employee, unless:

- That individual is an employee of the partnership, and

- The travel is for a bona fide business purpose and would otherwise be deductible by that individual.

Meals. Generally, the partnership can deduct only 50% of the amount otherwise allowable for non-entertainment meal expenses paid or incurred in its trade or business. However, the partnership can deduct 100% of business meals if the meals are food and beverages provided by a restaurant, and paid or incurred after

December 31, 2020, and before January 1, 2023. Entertainment-related meals are generally disallowed. In addition (subject to exceptions under section 274(k)(2)):

- Meals must not be lavish or extravagant, and
- A partner or employee of the partnership must be present at the meal.

See section 274(n)(3) for a special rule that applies to expenses for meals consumed by individuals subject to the hours of service limits of the Department of Transportation.

Membership dues. The partnership may deduct amounts paid or incurred for membership dues in civic or public service organizations, professional organizations (such as bar and medical associations), business leagues, trade associations, chambers of commerce, boards of trade, and real estate boards. However, no deduction is allowed if a principal purpose of the organization is to entertain, or provide entertainment facilities for, members or their guests. In addition, the partnership may not deduct membership dues in any club organized for business, pleasure, recreation, or other social purpose. This includes country clubs, golf and athletic clubs, airline and hotel clubs, and clubs operated to provide meals

under conditions favorable to business discussion.

Entertainment facilities. The partnership cannot deduct an expense paid or incurred for a facility (such as a yacht or hunting lodge) used for an activity usually considered entertainment, amusement, or recreation.

Amounts treated as compensation. Generally, the partnership may be able to deduct otherwise nondeductible entertainment, amusement, or recreation expenses if the amounts are treated as compensation to the recipient and reported on Form W-2 for an employee or on Form 1099-NEC for an independent contractor.

Reforestation expenditures. If the partnership made an election to deduct a portion of its reforestation expenditures on line 13d of Schedule K, it must amortize over an 84-month period the portion of these expenditures in excess of the amount deducted on Schedule K (see section 194).

Deduct on line 20 only the amortization of these excess reforestation expenditures. See *Reforestation expense deduction (code S),* later.

Tax and Payment

Line 23. Interest due under the look-back method for completed long-term contracts. For partnerships that aren't closely held, attach Form 8697 and a check or money order for the full amount, made payable to "United States Treasury." Write the partnership's EIN, daytime phone number, and "Form 8697 Interest'' on the check or money order.

Line 24. Interest due under the look-back method for property depreciated under the income forecast method. For partnerships that aren’t closely held, attach Form 8866 and a check or money order for the full amount, made payable to “United States Treasury.” Write the partnership’s EIN,

daytime phone number, and “Form 8866 Interest” on the check or money order.

Line 25. BBA AAR imputed underpayment. Use this line if the partnership is filing an AAR electronically and chooses to pay the imputed underpayment. For instructions on how to figure the imputed underpayment, see the Instructions for Form 8082. Write the name of the partnership, tax identification number, tax year, "Form 1065," and "BBA AAR Imputed Underpayment" on the payment. Checks must be made payable to “United States Treasury” and mailed to Ogden Service Center, Ogden, UT 84201-0011. Payments can be made by check or electronically. If making an electronic payment, choose the payment description “BBA AAR Imputed Underpayment” from the list of payment types.

Line 26. Other taxes. In a few instances, payments other than those listed above may have to be made with Form 1065. Enter the

amount on this line and attach a statement identifying the purpose of the payment.

Line 28. Payment. Enter any prepayments related to lines 23–26 above.

Schedule B. Other Information

Question 1

Check box 1f for any other type of entity and state the type.

Maximum Percentage Owned for Purposes of Questions 2 and 3

To determine the maximum percentage owned in the partnership's profit, loss, or capital for the purposes of questions 2a, 2b, and 3b, determine separately the partner's percentage of interest in profit, loss, and capital at the end of the partnership's tax year. This determination must be based on the partnership agreement and it must be

made using the constructive ownership rules described below. The maximum percentage is the highest of these three percentages (determined at the end of the tax year).

See *Item J. Partner's Profit, Loss, and Capital*, later, for more information on ownership percentages.

Questions 2 and 3

Constructive ownership of the partnership. For purposes of question 2, except for foreign governments within the meaning of section 892, in determining an ownership interest in the profit, loss, or capital of the partnership, the constructive ownership rules of section 267(c) (excluding section 267(c)(3)) apply to ownership of interests in the partnership as well as corporate stock. An interest in the partnership that is owned directly or indirectly by or for another entity (corporation, partnership, estate, trust, or tax-exempt organization) is

considered to be owned proportionately by the owners (shareholders, partners, or beneficiaries) of the owning entity.

Also, under section 267(c), an individual is considered to own an interest owned directly or indirectly by or for the individual’s family. The family of an individual includes only that individual's spouse, brothers, sisters, ancestors, and lineal descendants. An interest will be attributed from an individual under the family attribution rules only if the person to whom the interest is attributed owns a direct interest in the partnership or an indirect interest under section 267(c)(1) or (5). For purposes of these instructions, an individual will not be considered to own, under section 267(c)(2), an interest in the partnership owned, directly or indirectly, by a family member of the individual unless the individual also owns an interest in the partnership either directly or indirectly through a corporation, partnership, or trust.

For purposes of question 2, “foreign government” has the same meaning as it does under section 892. In determining a foreign government's ownership interest in the profit, loss, or capital of the partnership, the constructive ownership rules of Regulations section 1.892-5T(c)(1)(i) apply to ownership of interests in the partnership as well as corporate stock. An interest in the partnership that is owned directly or indirectly by an integral part or controlled entity of a foreign sovereign (within the meaning of Regulations section 1.892-2T(a)) is considered to be owned proportionately by such foreign sovereign.

Constructive ownership examples for questions 2 and 3 are included below. For the purposes of questions 2 and 3, add an owner's direct percentage ownership and indirect percentage ownership in an entity to determine if the owner owns, directly or indirectly, 50% or more of the entity.

Example for question 2a. Corporation A owns, directly, an interest of 50% in the profit, loss, or capital of Partnership B. Corporation A also owns, directly, an interest of 15% in the profit, loss, or capital of Partnership C. Partnership B owns, directly, an interest of 70% in the profit, loss, or capital of Partnership C. Therefore, Corporation A owns, directly or indirectly, an interest of 50% in the profit, loss, or capital of Partnership C (15% directly and 35% indirectly through Partnership B). On Partnership C's Form

1065, it must answer “Yes” to question 2a of Schedule B. See *Example 1* in the instructions attached to Schedule B-1 (Form 1065) for guidance on providing the rest of the information required of entities answering “Yes” to this question.

Example for question 2b. A owns, directly, 50% of the profit, loss, or capital of Partnership X. B, the daughter of A, doesn't

own, directly, any interest in X and doesn't own, indirectly, any interest in X through any entity (corporation, partnership, trust, or estate). Because family attribution rules apply only when an individual (in this example, B) owns a direct interest in the partnership or an indirect interest through another entity, A's interest in Partnership X isn't attributable to B. On Partnership X's Form 1065, it must answer “Yes” to question 2b of Schedule B. See *Example 2* in the instructions attached to Schedule B-1 (Form 1065) for guidance on providing the rest of the information required of entities answering “Yes” to this question.

Constructive ownership of other entities by the partnership. For purposes of determining the partnership's constructive ownership of other entities, the constructive ownership rules of section 267(c) (excluding section 267(c)(3)) apply to ownership of interests in partnerships and trusts as well as corporate stock. Generally, if an entity (a

corporation, partnership, or trust) is owned, directly or indirectly, by or for another entity (corporation, partnership, estate, or trust), the owned entity is considered to be owned proportionally by or for the owners (shareholders, partners, or beneficiaries) of the owning entity.

Question 3a. List each corporation in which the partnership, at the end of the tax year, owns, directly, 20% or more, or owns, directly or indirectly, 50% or more of the total voting power of all classes of stock entitled to vote. Indicate the name, EIN, country of incorporation, and percentage interest owned, directly or indirectly, in the total voting power. List the parent corporation of an affiliated group filing a consolidated tax return rather than the subsidiary members except for subsidiary members in which an interest is owned, directly or indirectly, independent of the interest owned, directly or indirectly, in the parent corporation. If a corporation is

owned through a DE, list the information for the corporation rather than the DE.

Question 3b. List each partnership in which the partnership, at the end of the tax year, owns, directly, an interest of 20% or more, or owns, directly or indirectly, an interest of 50% or more in the profit, loss, or capital of the partnership. List each trust in which the partnership, at the end of the tax year, owns, directly, an interest of 20% or more, or owns, directly or indirectly, an interest of 50% or more in the trust beneficial interest. For each partnership or trust listed, indicate the name, EIN, type of entity (partnership or trust), and country of origin. If the listed entity is a partnership, enter in column (v) the maximum of percentage interests owned, directly or indirectly, in the profit, loss, or capital of the partnership at the end of the partnership's tax year. If the entity is a trust, enter in column (v) the percentage of the partnership's beneficial interest in the trust

owned, directly or indirectly, at the end of the tax year. List a partnership or trust owned through a DE rather than the DE.

Question 4

Answer “Yes” if the partnership meets all four of the requirements shown on the form. Total receipts is defined as the sum of gross receipts or sales (page 1, line 1a); all other income (page 1, lines 4 through 7); income reported on Schedule K, lines 3a, 5, 6a, and 7; income or net gain reported on Schedule K, lines 8, 9a, 10, and 11; and income or net gain reported on Form 8825, lines 2, 19, and 20a. “Total assets” is defined as the amount that would be reported in item F on page 1 of Form 1065.

Question 5

Answer “Yes” if interests in the partnership are traded on an established securities market or are readily tradable on a secondary market (or its substantial equivalent).

Question 6

Generally, the partnership will have income if debt is canceled or forgiven. Amounts related to forgiven PPP loans are disregarded for purposes of this question. The determination of the existence and amount of cancellation of debt income is determined at the partnership level. Partnership cancellation of indebtedness income is separately stated on Schedule K and Schedule K-1. The extent to which such income is taxable is usually determined by each individual partner under rules found in section 108. For more information, see Pub. 334, Tax Guide for Small Business.

Question 7

Answer “Yes” if the partnership filed, or is required to file, a return under section 6111 to provide information on any reportable transaction by a material advisor. Use Form 8918, Material Advisor Disclosure Statement,

to provide the information. For details, see the Instructions for Form 8918.

Question 8

Answer “Yes” if either (1) or (2) below applies to the partnership. Otherwise, check the “No” box.

1. At any time during calendar year 2022, the partnership had an interest in or signature or other authority over a bank account, securities account, or other financial account in a foreign country (see FinCEN Form 114, Report of Foreign Bank and Financial

Accounts (FBAR)); and

- The combined value of the accounts was more than $10,000 at any time during the calendar year; and
- The accounts were not with a U.S. military banking facility operated by a U.S. financial institution.

2. The partnership owns more than 50% of the stock in any corporation that would answer “Yes” based on item (1) above. If the “Yes” box is checked for the question, do the following.

    - Enter the name of the foreign country or countries. Attach a separate sheet if more space is needed.
    - File FinCEN Form 114 electronically at the FinCEN website, *bsaefiling.fincen.treas.gov/main.html*.

Question 9

The partnership may be required to file Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, if any of the following apply.

- It directly or indirectly transferred property or money to a foreign trust. For this purpose, any U.S. person who

created a foreign trust is considered a transferor.

- It is treated as the owner of any part of the assets of a foreign trust under the grantor trust rules.
- It received a distribution, a loan of cash or other marketable securities, or uncompensated use of trust property from a foreign trust, or a foreign trust holds an outstanding qualified obligation of the partnership.

For more information, see the Instructions for Form 3520.

An owner of a foreign trust must ensure that the trust files an annual information return on Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner.

Questions 10a, 10b, and 10c

You must check "Yes" or "No" for each question.

Question 10a. Answer "Yes" if the partnership is making, or has made (and has not revoked), a section 754 election. For information about the election, see item 4 under *Elections Made by the Partnership*, earlier.

Question 10b. Answer "Yes" if the partnership made an optional basis adjustment under section 743(b) or 734(b) for the tax year. If the partnership has made a section 754 election (and it has not been revoked) and either of the following transactions occurs, the partnership must make a basis adjustment under section 734(b) or 743(b).

Section 743(b) basis adjustment. A section 743(b) basis adjustment is required if there is a transfer of an interest in the partnership by a sale or exchange, or in the death of a partner. See question 10c if the partnership has a substantial built-in loss immediately after such a transfer. The basis adjustment affects only the transferee's basis in partnership property. The partnership must attach a statement to the return for the tax year in which the transfer occurred. The statement must include:

- The name of the transferee partner,
- The EIN or SSN of the transferee partner,
- The computation of the adjustment, and
- The identity of the partnership properties to which the adjustment has been allocated.

For details, see section 743 and Regulations section 1.743-1. For details on allocating the basis adjustment to partnership properties, see section 755 and Regulations section 1.755-1.

Section 734(b) basis adjustment. A section 734(b) basis adjustment is required if there is a distribution of property to a partner, whether or not in liquidation of the partner's entire interest in the partnership. See question 10c if there is a substantial built-in loss related to the distribution. The basis adjustment affects each partner's basis in the partnership property. The partnership must attach a statement to the return for the tax year in which the distribution occurred. The statement must include:

- The computation of the adjustment,
- The class of property distributed (ordinary income property or capital gain property), and

- The partnership properties to which the adjustment has been allocated.

For details, see section 734 and Regulations section 1.734-1. For details on allocating the basis adjustment to partnership properties, see section 755 and Regulations section 1.755-1.

Question 10c. Answer "Yes" if the partnership had to make a basis reduction under section 743(b) because of a substantial built-in loss (as defined in section 743(d)) or under section 734(b) because of a substantial basis reduction (as defined in section 734(d)). Section 743(d)(1) provides that, for purposes of section 743, a partnership has a substantial built-in loss resulting from a transfer of a partnership interest if the partnership's adjusted basis in the partnership's property exceeds by more than $250,000 the FMV of the property or the transferee partner would be allocated a loss of more than $250,000 if the partnership

assets were sold for cash equal to their FMV immediately after such transfer. Under section 734(d), there is a substantial basis reduction resulting from a distribution if the sum of the following amounts exceeds $250,000.

- The amount of loss recognized by the distributee partner on a distribution in liquidation of the partner's interest in the partnership (see section 731(a)(2)).
- The excess of the basis of the distributed property to the distributee partner (determined under section 732) over the adjusted basis of the distributed property to the partnership immediately before the distribution (as adjusted by section 732(d)).

Section 743(b) basis adjustment. For a section 743(b) basis adjustment, attach a statement that includes:

- The name of the transferee partner,
- The EIN or SSN of the transferee partner,
- The computation of the adjustment, and
- The identity of the partnership properties to which the adjustment has been allocated.

Section 734(b) basis adjustment. For a section 734(b) basis adjustment, attach a statement that includes:

- The computation of the adjustment,
- The class of property distributed (ordinary income property or capital gain property), and
- The partnership properties to which the adjustment has been allocated.

Question 11

Check the box if the partnership engaged in a like-kind exchange during the current or immediately preceding tax year and received replacement property that it distributed during the current tax year. For purposes of this question, the partnership is considered to have distributed replacement property if the partnership contributed such property to any entity other than a DE. The distribution of its ownership interest in a DE is considered a distribution of the underlying property.

Question 12

If a partnership distributed property to its partners to be jointly owned, whether such distribution is direct or through the formation of an intermediate entity, the question must be answered "Yes." For purposes of question 12, an "undivided interest in partnership property" means property that was owned by the partnership either directly or through a

DE and which was distributed to partners as fractional ownership interests. A tenancy-in-common interest is a type of undivided ownership interest in property which provides each owner the right to transfer property to a third party without destroying the tenancy in common. Partners may agree to partition property held as tenants in common or may seek a court order to partition the property (usually dividing the property into fractional interests in accordance with each partner's ownership interest in the partnership).

Example. Partnership P is a partnership that files Form 1065. Partnership P holds title to land held for investment. Partnership P converts its title to the land to fractional interests in the name of the partners and distributes such interests to its partners. Partnership P must answer “Yes” to question 12.

Question 13

Enter the number of Forms 8858, Information Return of U.S. Persons With Respect To Foreign Disregarded Entities (FDEs) and Foreign Branches (FBs), that are attached to the return. Form 8858 and its schedules are used by certain U.S. persons (including domestic partnerships) that own an FDE or FB directly (or, in certain cases, indirectly or constructively) to satisfy the reporting requirements of sections 6011, 6012, 6031, and 6038, and the related regulations. See Form 8858 (and its separate instructions) for information on completing the form and the information that the partnership may need to provide to certain partners for them to complete their Forms 8858 relating to that FDE or FB.

Question 14

Answer “Yes” if the partnership had any foreign partners (for purposes of section

1446(a)) at any time during the tax year. Otherwise, answer "No."

If the partnership had gross income effectively connected with a trade or business in the United States and foreign partners, it may be required to withhold tax under section 1446(a) on income allocable to foreign partners (without regard to distributions) and file Forms 8804, 8805, and 8813. See Regulations sections 1.1446-1 through -7 for more information.

Questions 16a and 16b

If the partnership made any payment in 2022 that would require the partnership to file any Form(s) 1099, check the "Yes" box for question 16a and answer question 16b. Otherwise, check the "No" box for question 16a and skip question 16b. See *Am I Required to File a Form 1099 or Other Information Return* for more information.

Question 20

For tax years beginning after 2015, domestic partnerships that are formed or availed of to hold specified foreign financial assets ("specified domestic entities") must file Form 8938, Statement of Specified Foreign Financial Assets, with its Form 1065 for the tax year. Form 8938 must be filed each year the value of the partnership's specified foreign financial assets meets or exceeds the reporting threshold. For more information on domestic partnerships that are specified domestic entities and the types of foreign financial assets that must be reported, see the Instructions for Form 8938.

A domestic partnership required to file Form 8938 with its Form 1065 for the tax year should check "Yes" to question 20 on Schedule B of Form 1065.

Question 22

Section 267A disallows a deduction for certain interest or royalty paid or accrued pursuant to a hybrid arrangement, to the extent that, under the foreign tax law, there is not a corresponding income inclusion (including long-term deferral). Report on line 22 the total amount of interest and royalty paid or accrued by the partnership for which the partnership knows, or has reason to know, that one or more partners' distributive share of deductions is disallowed under section 267A. For additional information, see FAQs at *IRS.gov/ businesses/partnerships/FAQs-for-Form-1065-Schedule-B-OtherInformation-Question-22*.

Question 23

The limitation on business interest expense applies to every taxpayer with a trade or business, unless the taxpayer meets certain specified exceptions. A partnership may elect

out of the limitation for certain businesses otherwise subject to the business interest expense limitation.

Certain real property trades or businesses and farming businesses qualify to make an election not to limit business interest expense. This is an irrevocable election. If you make this election, you are required to use the alternative depreciation system to depreciate certain property. Also, you are not entitled to the special depreciation allowance for that property. For a partnership with more than one qualifying business, the election is made with respect to each business. Check "Yes" if the partnership has an election in effect to exclude a real property trade or business or a farming business from section 163(j). For more information, see section 163(j) and the Instructions for Form 8990.

Question 24

Generally, a taxpayer with a trade or business must file Form 8990 to claim a deduction for business interest. Business interest expense is interest that is properly allocable to a non-excepted trade or business or that is floor plan financing interest. In addition, Form 8990 must be filed by any taxpayer that owns an interest in a partnership with current year, or prior year carryover, excess business interest expense allocated from the partnership. A pass-through entity allocating excess taxable income or excess business interest income to its owners (that is, a pass-through entity that isn't a small business taxpayer) must file Form 8990, regardless of whether it has any interest expense.

Exclusions from filing. A taxpayer isn't required to file Form 8990 if the taxpayer is a small business taxpayer and doesn't have excess business interest expense from a partnership. A taxpayer is also not required to

file Form 8990 if the taxpayer only has business interest expense from the following excepted trades or businesses.

- The trade or business of providing services as an employee.
- An electing real property trade or business.
- An electing farming business.
- Certain utility businesses.

Small business taxpayer. A small business taxpayer isn't subject to the business interest expense limitation and isn't required to file Form 8990. A small business taxpayer is a taxpayer that (a) isn't a tax shelter (as defined in section 448(d)(3)); and (b) meets the gross receipts test of section 448(c), discussed next.

Gross receipts test. A taxpayer meets the gross receipts test if the taxpayer has average annual gross receipts of $27 million

or less for the 3 prior tax years. A taxpayer's average annual gross receipts for the 3 prior tax years is determined by adding the gross receipts for the 3 prior tax years and dividing the total by 3. Gross receipts include the aggregate gross receipts from all persons treated as a single employer, such as a controlled group of corporations, commonly controlled partnerships, or proprietorships, and affiliated service groups. See section 448(c) and the Instructions for Form 8990 for additional information.

Question 25

To be certified as a qualified opportunity fund, the partnership must file Form 1065 and attach Form 8996, even if the partnership had no income or expenses to report. If the partnership is attaching Form 8996, check the "Yes" box for question 26. On the line following the dollar sign, enter the amount from Form 8996, line 15.

Question 26

Provide the number of foreign partners subject to section 864(c)(8) as a result of transferring all or a portion of an interest in the partnership if the partnership is engaged in a U.S. trade or business. Section 864(c)(8) provides that gain or loss of a foreign transferor from the transfer of a partnership interest is treated as effectively connected with the conduct of a trade or business within the United States to the extent that the transferor would have had effectively connected gain or loss if the partnership sold all of its assets at FMV on the date of transfer. For purposes of section 864(c)(8), a transfer of a partnership interest means a sale, exchange, or other disposition, and includes a distribution from a partnership to a partner to the extent that gain or loss is recognized on the distribution, as well as a transfer treated as a sale or exchange under section 707(a)(2)(B). Section 864(c)(8)

applies to foreign partners that directly or indirectly transfer an interest in a partnership that is engaged in a U.S. trade or business. The partnership should include in its response any transfer for which it has received notification or otherwise knows about. If the partnership is a PTP as defined in section 469(k)(2) and has properly answered “Yes” to question 5 on Form 1065, Schedule B, then it is not required to answer the question.

If a partnership had any foreign partners subject to section 864(c) (8), the partnership must complete Schedule K-3 (Form 1065), Part XIII, for each foreign partner subject to section 864(c)(8) on a transfer or distribution. The partnership may also be required to withhold under section 1446(f)(4) on future distributions that it makes to the transferee partner if that partner failed to withhold on the transfer under section 1446(f)(1). See Pub. 515, Withholding of Tax

on Nonresident Aliens and Foreign Entities, for more information.

Question 27

Answer "Yes" if at any time during the tax year there were transfers between the partnership and its partners subject to the disclosure requirements of Regulations section 1.707-8. For certain transfers that are presumed to be sales, the partnership or the partners must comply with the disclosure requirements in Regulations section 1.707-8. Generally, disclosure is required when:

1. Certain transfers to a partner are made within 2 years of a transfer of property by the partner to the partnership;
2. Certain debt is incurred by a partner within 2 years of the earlier of (a) a written agreement to transfer, or (b) a transfer of the property that secures

the debt, if the debt is treated as a qualified liability; or

3. Transfers from a partnership to a partner occur which are the equivalent to those listed in (1) or (2) above.

The disclosure must be made on the transferor partner's return using Form 8275, Disclosure Statement, or on an attached statement providing the same information. When more than one partner transfers property to a partnership under a plan, the disclosure may be made by the partnership rather than by each partner.

Question 28

Section 7874 applies in certain cases in which a foreign corporation directly or indirectly acquires substantially all of the properties constituting a trade or business of a domestic partnership. Check “Yes” if, since December 22, 2017, a foreign corporation directly or indirectly acquired substantially all of the

properties constituting a trade or business of your partnership (and you are a domestic partnership), and the ownership with respect to the acquisition was greater than 50% (by vote or value). If “Yes” is checked, list the ownership percentage by both vote and value.

The information must be reported even if you conclude that section 7874 does not apply.

Section 7874 generally applies when the following three requirements are met.

1. Pursuant to a plan or series of related transactions, a foreign corporation must acquire directly or indirectly substantially all of the properties constituting a trade or business of a domestic partnership.
2. After the acquisition, the ownership percentage (by vote or value) must be at least 60%.
3. After the acquisition, the expanded affiliate that includes the foreign

acquiring corporation must not have substantial business activities in the foreign country in which the foreign acquiring corporation is created or organized.

When section 7874 applies, the tax treatment of the acquisition depends on the ownership percentage. If the ownership is at least 80%, the foreign acquiring corporation is treated as a domestic corporation for all purposes of the Internal Revenue Code. See section 7874(b). If the ownership is at least 60% but less than 80%, the foreign acquiring corporation is considered a foreign corporation but the domestic partnership and certain other persons are subject to special rules that reduce the tax benefits of the acquisition. See section 7874(a)(1).

The Tax Cuts and Jobs Act of 2017 provides additional special rules for certain cases in which section 7874 applies. See sections 59A(d)(4) and 965(l).

Ownership percentage. The ownership percentage is the percentage described in section 7874(a)(2)(B)(ii). See the regulations under section 7874 for rules regarding the computation of the ownership percentage.

In general, the ownership percentage measures the percentage of stock of the foreign acquiring corporation that is held by partners of the domestic partnership by reason of holding a capital or profits interest in the domestic partnership, with certain adjustments (for example, disregarding certain stock of the foreign acquiring corporation attributable to passive assets or assets of other domestic entities that were recently acquired by the foreign acquiring corporation). The ownership percentage is measured separately by vote and value.

Multiple reportable acquisitions. If there are multiple acquisitions that must be reported, list on the lines for question 28 the ownership percentage by vote and value for

the most recent acquisition. Attach a statement reporting the ownership percentage by vote and value for the other acquisitions.

Question 29

Reserved for future use.

Question 30

Answer "Yes" if an eligible partnership chooses to elect out of the centralized partnership audit regime for the tax year and enter the total from Schedule B-2, Part III, line 3. If making the election, attach a completed Schedule B-2 to Form 1065. An election out of the centralized partnership audit regime can only be made on a timely filed return (including extensions). A partnership is an eligible partnership for the tax year if it has 100 or fewer eligible partners in that year. Eligible partners are individuals, C corporations, S corporations, foreign entities that would be C corporations

if they were domestic entities, and estates of deceased partners. The determination as to whether the partnership has 100 or fewer partners is made by adding the number of Schedules K-1 required to be issued by the partnership for the tax year to the number of Schedules K-1 required to be issued by any partner that is an S corporation to its shareholders for the tax year of the S corporation ending with or within the partnership tax year. A partnership isn't eligible to elect out of the centralized partnership audit regime if it is required to issue a Schedule K-1 to any of the following partners.

- A partnership.
- A trust.
- A foreign entity that would not be treated as a C corporation if it were a domestic entity.
- A DE described in Regulations section 301.7701-2(c)(2)(i).

- An estate of an individual other than a deceased partner.
- Any person that holds an interest in the partnership on behalf of another person.

Designated Partnership Representative (PR)

Section 6223 provides that unless the partnership has made a valid election out of the centralized partnership audit regime, each partnership must designate, in the manner prescribed by the Secretary, a partner or other person with a substantial presence in the United States as the PR who shall have the sole authority to act on behalf of the partnership. On Form 1065, provide the name, address, and phone number of the PR. If an entity is designated as the PR, the partnership must also appoint an individual to act on the entity's behalf (a designated individual (DI)). To be a DI, the appointed

person must also have a substantial presence in the United States.

How to designate. A designation of a PR must be made for each respective year on the partnership's Form 1065. The partnership can revoke a designation of a PR or DI, and the PR or DI can resign, by submitting Form 8979, Partnership Representative Revocation, Designation, and Resignation Form.

See the Instructions for Form 8979 for information concerning how and when Form 8979 can be submitted to the IRS.

PR authority. Under section 6223, the partnership and all its partners (and any other person whose tax liability is determined in whole or in part by taking into account directly or indirectly adjustments determined under the centralized partnership audit regime) are bound by the actions of the PR in dealings with the IRS. A designation for a partnership tax year remains in effect until

the designation is terminated by (a) a valid resignation of the PR or DI, (b) a valid revocation of the PR (with designation of successor PR), or (c) a determination by the IRS that the designation isn't in effect.

Substantial presence. In order for either a PR or a DI to have substantial presence, they must make themselves available to meet in person with the IRS in the United States at a reasonable time and place as determined by the IRS, and must have a street address in the United States, a U.S. taxpayer identification number (TIN), and a telephone number with a U.S. area code.

Schedules K and K-1. Partners' Distributive Share Items

Purpose of Schedules

Although the partnership isn't subject to income tax, the partners are liable for tax on

their shares of the partnership income, whether or not distributed, and must include their shares on their tax returns.

Schedule K. Schedule K is a summary schedule of all the partners' shares of the partnership's income, credits, deductions, etc. All partnerships must complete Schedule K. Rental activity income (loss) and portfolio income aren't reported on page 1 of Form 1065. These amounts aren't combined with trade or business activity income (loss) reported on page 1. Schedule K is used to report the totals of these and other amounts reported on page 1.

Schedule K-1. Schedule K-1 shows each partner's separate share. Attach a copy of each Schedule K-1 to the Form 1065 filed with the IRS. Keep a copy with a copy of the partnership return as a part of the partnership's records and furnish a copy to each partner. If the partner is a DE, furnish the Schedule K-1 to the DE partner. If a

partnership interest is held by a nominee on behalf of another person, the partnership may be required to furnish Schedule K-1 to the nominee. See Temporary Regulations sections 1.6031(b)-1T and 1.6031(c)-1T for more information.

Give each partner a copy of either the Partner's Instructions for Schedule K-1 (Form 1065) or specific instructions for each item reported on the partner's Schedule K-1.

Note. Schedules K-2 and K-3 replace prior lines 16 and 20 for certain international codes on Schedules K and K-1.

Substitute Forms

The partnership doesn't need IRS approval to use a substitute Schedule K-1 if it is an exact copy of the IRS schedule. The boxes must use the same numbers and titles and must be in the same order and format as on the comparable IRS Schedule K-1. The substitute schedule must include the OMB number.