

Guidance on Special Enforcement Matters Under the Centralized Partnership Audit Regime

Notice 2019-06

SECTION 1. PURPOSE

This notice informs taxpayers that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) intend to propose regulations addressing certain special enforcement matters under section 6241(11). This notice also requests comments regarding other special enforcement matters that could be the subject of future proposed regulations.

SECTION 2. BACKGROUND

Section 206(l) of the Technical Corrections Act of 2018, contained in Title II of Division U of the Consolidated Appropriations Act of 2018, Public Law 115-141 (TTCA), added section 6241(11) to the Internal Revenue Code (Code), regarding the treatment of special enforcement matters. Under section 6241(11), in the case of partnership-related items involving special enforcement matters, the Secretary may prescribe regulations providing that the centralized partnership audit regime (or any portion thereof) does not apply to such items and that such items are subject to special rules as the Secretary determines to be necessary for the effective and efficient enforcement of the Code. For purposes of section 6241(11), the term “special enforcement matters” means: (1) failure to comply with the requirements of section 6226(b)(4)(A)(ii) (regarding the requirement for a partnership-partner or S corporation partner to furnish statements

or compute and pay an imputed underpayment); (2) assessments under section 6851 (relating to termination assessments of income tax) or section 6861 (relating to jeopardy assessments of income, estate, gift, and certain excise taxes); (3) criminal investigations; (4) indirect methods of proof of income; (5) foreign partners or partnerships; and (6) other matters that the Secretary determines by regulation present special enforcement considerations.

Section 6221(a) requires that any adjustment to a partnership-related item shall be determined at the partnership level under the centralized partnership audit regime, except to the extent otherwise provided in subchapter C of chapter 63 of the Code. A partnership-related item is defined in section 6241(2) as any item or amount with respect to the partnership which is relevant in determining the tax liability of any person under chapter 1 of the Code, including any distributive share of such an item or amount.

Certain partnerships may elect out of the centralized partnership audit regime under section 6221(b). A partnership is eligible to make an election out if it has 100 or fewer partners for the taxable year, each partner in the partnership is an eligible partner, the election is timely made in the manner prescribed by the Secretary, and the partnership notifies its partners of the election in the manner prescribed by the Secretary. The number of partners is determined by counting the number of statements required to be furnished by the partnership under section 6031(b) and the number of statements required to be furnished by any S corporation partners of the partnership. Eligible partners are prescribed in section 6221(b)(1)(C) and Treas. Reg. §301.6221(b)-1(b)(3)(i), and include C corporations.

A qualified subchapter S subsidiary (QSub) is defined in section 1361(b)(3) as a domestic corporation that has 100 percent of its stock held by an S corporation and for which an election has been made to treat it as a QSub. Except as provided by regulation, a QSub is not treated as a corporation separate from its S corporation shareholder and its assets, liabilities, and items of income, deduction and credit are treated as the assets, liabilities, and items of its S corporation shareholder for the taxable year. Section 1361(b)(3)(A). For purposes of the Code, a C corporation is defined under section 1361(a)(2) as a corporation which is not an S corporation. Because a QSub is not an S corporation, it is a C corporation (as defined in section 1361(a)(2)). Because a QSub is a C corporation, it is an eligible partner under section 6221(b).

SECTION 3. GUIDANCE TO BE ISSUED

The Treasury Department and the IRS intend to propose regulations under section 6241(11)(B)(vi) regarding two matters that the Secretary has determined present special enforcement considerations. The first matter concerns certain situations in which an adjustment during an examination of a person other than the partnership requires a change to a partnership-related item. Specifically, the regulations will allow the IRS to effectively and efficiently focus on a single partner or a small group of partners with respect to a limited set of partnership-related items without unduly burdening the partnership and avoiding procedural concerns about the appropriate level at which such items must be examined. Consequently, the regulations will provide that the IRS may determine that the centralized partnership audit regime does not apply to adjustments to partnership-related items when the following conditions are met:

(1) The examination being conducted is of a person other than the partnership;

(2) A partnership-related item must be adjusted, or a determination regarding a partnership-related item must be made, as part of an adjustment to a non-partnership-related item of the person whose return is being examined; and

(3) The treatment of the partnership-related item on the return of the partnership under section 6031(b) or in the partnership's books and records was based in whole or in part on information provided by, or under the control of, the person whose return is being examined.

The second matter concerns situations where a QSub is a partner in a partnership. The regulations will provide that this situation presents special enforcement considerations because partnership structures with QSubs as partners could have far more than 100 ultimate partners, including many thousands, and still potentially elect out of the centralized partnership audit regime. Allowing such a large partnership to elect out of the centralized partnership audit regime would give rise to significant enforcement concerns for the IRS and frustrate the efficiencies introduced by the centralized partnership regime. As a result, the regulations will provide that section 6221(b) generally does not apply to a partnership with a QSub as a partner. The regulations will also provide, however, that if a partnership meets certain requirements as set forth in the regulations, the partnership may make an election under section 6221(b). Specifically, the regulations will apply a rule similar to the rules for S corporations under section 6221(b)(2)(A). The regulations will also provide that for purposes of determining whether a partnership has 100 or fewer partners for the taxable

year for purposes of the election under section 6221(b), the partnership must include (1) the statement the partnership is required to furnish to the QSub partner under section 6031(b) and (2) each statement the S corporation that holds 100 percent of the stock of the QSub partner is required to furnish to its shareholders under section 6037(b).

The Treasury Department and the IRS intend to issue proposed and final regulations prior to eighteen months after enactment of the TTCA such that the intended regulations described in this section of the Notice may be applicable to all partnership taxable years beginning after December 31, 2017. Section 7805(b)(2). If final regulations are not issued prior to eighteen months after enactment of the TTCA, the Treasury Department and the IRS intend the regulations to be applicable to partnership taxable years beginning after December 31, 2017 and ending after the date this Notice is issued to the public. Section 7805(b)(1)(C).

SECTION 4. REQUEST FOR COMMENTS

The Treasury Department and the IRS request comments on the intended regulations described in section 3 of this notice and whether any other matters might present special enforcement matters under section 6241(11). Comments must be received by February 22, 2019.

SECTION 5. ADDRESS TO SEND COMMENTS

Taxpayers may submit comments electronically via the Federal eRulemaking Portal at www.regulations.gov (type IRS-2018-0044 in the search field on the regulations.gov homepage to find this notice and submit comments). All

recommendations for guidance submitted by the public in response to this notice will be available for public inspection and copying in their entirety.

Alternatively, taxpayers may mail comments to:

Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2019-06) Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

or hand deliver comments Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

Courier's Desk
Internal Revenue Service
Attn: CC:PA:LPD:PR (Notice 2019-06)
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

SECTION 6. DRAFTING INFORMATION

The principal author of this notice is Jennifer M. Black of the Office of the Associate Chief Counsel (Procedure and Administration). For further information regarding this notice, contact Ms. Black at (202) 317-6834 (not a toll-free call).