Time to Pay the Piper: New Partnership Audit Rules and the Impact on Entities of All Sizes

American Institute of Certified Public Accountants
Bipartisan Budget Act of 2015

- Repeals TEFRA (1982 Tax Equity and Fiscal Responsibility Act) rules
- Creates entirely new Audit and Assessment Regime
- New rules generally effective for tax years beginning after 12/31/17
New Terms of Art

- Imputed Underpayment
- Reviewed Year
- Adjustment Year
- Partnership Representative
Partnership Representative

• Must be “person” with substantial U.S. presence
• Need not be a partner
• If none designated, IRS will appoint one
• Receives all notices, makes all decisions, is “all-powerful”
Small Partnership Opt-out Election

- Available only if 100 or fewer eligible partners
- No partner may be a partnership, LLC, LLP, or trust
- Special rules for S Corporations as partners
- Election must be made annually on each year’s timely filed original return
Default Rules

- All adjustments determined at partnership level
- Penalties determined at partnership level
- Partnership pays assessment – calculated using highest rate in reviewed year (i.e. - 39.6%)
- Statute of limitations applied only at partnership level
Available Adjustments to Reduce Partnership Level Tax

- Reviewed Year partners file amended returns
- Prove that adjustment relates to Tax-Exempt partner, C Corporation partner or is eligible for capital gains rate
- Special rules for PTPs with passive losses
- Provide proof to IRS within 270 days - IRS must approve any adjustments
The “Push-Out” Option

- Must elect within 45 days after final determination
- Issue “adjustment K-1s” to Reviewed Year partners
- Partner calculates and pays additional tax with current year return
- Interest rate is bumped up 2%
Administrative Adjustment Requests

• No more Amended Returns (Form 1065-X)
• AAR must be filed within 3 year Statute period
• If results in underpayment, can pay using either default or “push-out” methods
• If results in overpayment, MUST use “push-out” method
Assessment Stage Issues

• If audit results in overpayment, NO refund issued, partnership adjusts current year
• Must file AAR and use “push-out” option
• Adjustments to allocation between partners NOT netted
• If amended returns filed – all partners affected by allocation must file
Partnership Issues & Concerns

- Who selects Partnership Representative?
- How and when can they be replaced?
- Require approval by all or some partners for his decisions?
- Limit number/type of partners to be eligible for opt-out?
Partnership Issues & Concerns

- Require notice to partners of proceedings in agreement?
- Require reviewed year partners to amend returns?
- What if partnership has ceased to exist?
- How does all this work with tiered partnerships?
State Level Considerations

- What information will be shared by IRS?
- Can they collect directly from partnerships?
- If no audit of partner, can they require amended return?
- What’s the effect on resident/non-resident partners – composite return filings?
IRS Guidance

• Notice 2016-23 issued March 4th
• Multiple additional notices along with temporary and proposed regulations expected in coming months
• Possibility of some legislative “fixes” as well
Start Preparing Today

- Discuss issues with partnership clients
- Have partnership agreements reviewed for potential changes
- Consider changes in partners/partnership structure to become eligible for “opt-out”