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From: [REDACTED]

Sent: Tuesday, October 15, 2019 3:01:59 PM

To: [REDACTED]

Cc: [REDACTED]

Bcc:

Subject: Adjustments to a taxpayer who is deemed an owner of partnership interests

You have requested advice on whether a change in the identity of a partner in the partnership described below is a “partnership item” that would require a separate audit proceeding with respect to that partnership. During the taxable years in issue, the partnership unified audit and litigation procedures in effect were the procedures enacted by the Tax Equity and Fiscal Responsibility Act of 1982. Pub. L. 97-248, § 402, 96 Stat. 648 (1982).

The facts are as follows. Taxpayer is a U.S. person that is treated as a partnership for U.S. federal tax purposes. To retain investment exposure to HF, a hedge fund that is treated as a partnership for U.S. federal tax purposes and that holds a diversified pool of other hedge fund interests, Taxpayer entered into contracts (“Contracts”) with a counterparty bank (“Bank”) referencing partnership interests in HF (“HF Interests”). Taxpayer and Bank accounted for the transaction as though the Contract was a derivative and treated Bank as the owner of the HF Interests. As a result, during the taxable years at issue, Bank treated itself as the partner in HF and reported items of income, expense, gain, and loss that HF reported to its partners on Schedules K-1. Exam has concluded that, for tax purposes, Taxpayer owns the HF interests and Taxpayer (and not Bank) is the true partner in HF. As a result, exam proposes to make adjustments to Taxpayer’s Form 1065 (U.S. Return of Partnership Income) to include partnership items that HF reported to Bank on Schedule K-1.

You have asked whether these adjustments require separate partnership unified audit and litigation procedures with respect to HF. The identity of Taxpayer versus Bank as the partner in HF is not a partnership item because the determination will not affect the distributive shares of HF’s other partners. See *Blonien v. Commissioner*, 118 T.C. 541, 551 fn. 6 (2002) (“determination of who is a partner can be a partner-level item where resolution of the issue would not affect the allocation of partnership items to the other partners”); *Hang v. Commissioner*, 95 T.C. 74, 80 (1990) (considering benefits and burden of ownership because reallocation of income from S corporation’s shareholders of record to taxpayer who is not a shareholder of record is not a partnership item). Accordingly, adjustments to Taxpayer’s Forms 1065 that reflect inclusion of partnership items from HF’s Schedule K-1 do not require that a separate audit proceeding be opened with respect to HF.

Please call if you have any additional questions.