



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: DEBORAH A. BUTLER
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SUBJECT: Assessing Tentative Carryback Adjustments in TEFRA
Cases

This Field Service Advice responds to your memorandum dated June 16, 1998 and is to supplement our response dated September 25, 1998. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND

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ISSUE

Whether the TEFRA¹ restriction on assessment prohibits the assessment and collection of tax attributable to the disallowance of a tentative carrybacks claimed under I.R.C. § 6411.

CONCLUSION

¹Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248.

In limited situations, tax attributable to the disallowance of a tentative carryback claimed under I.R.C. § 6411 may be assessed, without regard to the I.R.C. § 6225 restriction on assessment.

FACTS

The facts are sufficiently set forth in prior correspondence in this matter, and are repeated only to the extent they relate to the limited issue discussed herein. A is a series of related partnerships. Most of these partnerships are subject to the TEFRA unified audit and litigation procedures; although some partnerships fall outside the purview of TEFRA. Many of the partnerships reported distributive shares of losses to the partners, and the partners claimed the losses on their returns. To the extent the losses could be carried back to other taxable years, many partners claimed tentative carryback adjustments pursuant to I.R.C. § 6411. Subsequent examination of the partnerships has resulted in the issuance of notices of final partnership administrative adjustment which, if sustained, would result in the disallowance of the losses and, in turn, the carryback adjustments.² The Service seeks to assess and collect the tax attributable to the tentative carryback adjustments prior to the conclusion of the TEFRA proceeding.

LAW AND ANALYSIS

Generally, the assessment and collection of income tax is restricted by I.R.C. § 6213, which prohibits assessment or collection of a deficiency until after the issuance of a notice of deficiency and the lapse of the petition period. If a petition is filed, assessment and collection are further restricted for the period until a decision of the Tax Court becomes final. This restriction is lifted in the case of adjustments attributable to the disallowance of a tentative carryback adjustment. I.R.C. § 6213(b)(3). Accordingly, for partners in non-TEFRA partnerships, we may assess adjustments based upon the disallowance of the tentative carryback adjustment without regard to the I.R.C. § 6213(a) restriction on assessment. However, the answer is somewhat different for partners in TEFRA partnerships.

In 1982, Congress enacted the TEFRA unified audit and litigation procedures to simplify and streamline the partnership audit, litigation, and assessment process. The underlying principle of TEFRA is that "the tax treatment of items of partnership income, loss, deductions, and credits will be determined at the partnership level in a unified partnership proceeding rather than separate proceedings with the

²For those partnerships not subject to TEFRA, statutory notices of deficiency disallowing the losses were issued to the partners.

partners."³ Accordingly, the Service may examine the partnership as an entity, rather than conduct a separate examination as to each of the partners.

Despite the creation of a unified procedure for audit and litigation, the manner of tax reporting and assessment is not affected by TEFRA and it is the partners that are the true subject of a TEFRA proceeding. With regard to restrictions on assessment, the TEFRA provisions contain a separate provision which prohibits the assessment or collection of tax attributable to the adjustment of partnership items for the period during which a partner could file a petition from a notice of final partnership administrative adjustment or, if a petition is filed, until a decision of the Tax Court becomes final. I.R.C. § 6225(a). With regard to tentative carryback adjustments, I.R.C. § 6225 does not contain an exception similar to that provided by I.R.C. § 6213(c). However, Congress vested the Secretary with broad authority to promulgate regulations "necessary to carry out the purposes of this subchapter." I.R.C. § 6230(k). Furthermore, Congress granted even broader regulatory authority with regard to "special enforcement areas." See I.R.C. § 6231(c)(3).

Under the authority to issue regulations in special enforcement areas, the Secretary promulgated special rules for assessment in the event of the disallowance of a tentative carryback adjustment. See generally, Temp. Treas. Reg. § 301.6231(c)-1T. If it is determined that any person who organized the partnership made a gross valuation overstatement or a false or fraudulent statement with regard to the tax benefits of the partnership that would subject such person to a penalty for promoting an abusive tax shelter, the restriction against assessment and collection is lifted for tentative carryback adjustments, subject to special rules. Temp. Treas. Reg. § 301.6231(c)-1T(a). In such a situation, the Service must mail a "math error notice" informing the partner of the assessment and of the partner's limited right to treat the partnership items as nonpartnership items. Temp. Treas. Reg. § 301.6231(c)-1T(c). The partner then has the right to elect to treat all partnership items of the source year as nonpartnership items. Temp. Treas. Reg. § 301.6231(c)-1T(d). It should be noted, however, that this right cannot be exercised after the issuance of a notice of final partnership administrative adjustment. Temp. Treas. Reg. § 301.6231(c)-1T(d)(2)(ii).

In the present matter, the FPAA has already been mailed. Accordingly, the taxpayers would not be able to convert their partnership items to nonpartnership items. Though this result may seem harsh, this is the result intended by the regulations. The regulations allow taxpayers to convert their partnership items to nonpartnership items only in the situation in which there would be no judicial forum to review the adjustment. In situations in which an AAR resulted in the carryback,

³Conf. Rep. No. 97-248 at 600 (1982), 1982-2 C.B. 462.

and in which a judicial forum is granted pursuant to I.R.C. § 6228, the tentative carryback provision is rendered inapplicable. I.R.C. § 6231(c)-1T(a). Similarly, if an FPAA is issued, the determinations contained therein may be judicially reviewed pursuant to I.R.C. § 6226. Only in the situation in which the loss stemmed from the original partnership return and no FPAA was issued would the parties be deprived of a judicial forum in which to contest the disallowance. Accordingly, it is only in this situation that the partner may elect to convert the partnership items to nonpartnership items. Because this situation is not present, the loss may be disallowed and the only remedy for the partner is to pursue the underlying merits in the docketed Tax Court case.

If you have any further questions, please call (202) 622-7950.

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