

Tax Notes

IRS Re-Releases New Partnership Audit Rules — What Now?

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The Internal Revenue Service (“IRS”) re-released the proposed new partnership audit rules and guidance. The IRS originally issued these proposed regulations on January 18, 2017 and withdrew them on January 20, 2017, only to reissue them on June 13, 2017. These new rules are effective for partnerships with tax years beginning after December 31, 2017, as outlined in our prior newsletter [The New Partnership Tax Audit Rules: Are You Prepared for Change in 2018?](#)

The newly released, re-issued regulations contain two minor changes: (1) the removal of an example dealing with the netting of income and depreciation expense, and (2) an expanded section about allowing tiered partnerships to pass through certain adjustments to individual partners. The balance of the re-issued regulations remain intact similar to the version issued in January 2017.

The IRS asked for written comments to the proposed regulations by August 14, 2017 and already has scheduled a public hearing for September 18, 2017.

In Brief

This new and more streamlined partnership audit regime was enacted in November 2015 by the Bipartisan Budget Act (“BBA”) of 2015 and subsequently amended in December 2015 by the Protecting Americans from Tax Hikes (“PATH”) Act of 2015. This legislation repealed the partnership audit rules of the Tax Equity and Fiscal Responsibility Act (“TEFRA”) of 1982. These proposed new rules apply to **ALL** partnerships and significantly change how partnership adjustments are determined and passed through to the ultimate partners of the partnership.

Under these new partnership audit rules, any imputed underpayment of taxes will be assessed at the top corporate or individual tax rate and paid at the partnership level. Importantly, the IRS will assess the partnership in the year of the adjustment — when the examination ends — as opposed to the year being reviewed. These rules will materially change how partnerships are audited and how the IRS will assess and collect its tax as all tax assessed will now be centralized at the partnership level.

The proposed regulations address a variety of topics including: (a) the applicability and scope of the new partnership regime, (b) procedural rules dealing with electing-out and electing-in of the new BBA rules, (c) filing administrative adjustment requests, (d) determining actual amounts owed by a partnership under the new regime, (e) the role of the partnership representative, and (f) notice rights of the partners.

What Now?

With respect to these new rules and preparing for what’s on the horizon, here are some things to consider when revising your partnership agreements — or to look out for when investing in new ones:

- Review the BBA, its regulations and application with your advisors and members of management.

- Carefully select and work toward defining the roles and responsibilities of the partnership representative. This individual will have a significant role in the examination process; therefore, the selection should be approached with care and caution.
- Address how to allow the partnership to have its partners (past, present and future) share fairly in any partnership level tax liability resulting from examination.
- Consider the types (i.e., individual, trust and entity) and number of partners allowed to enter the entity.
- Consider specifying notice and participation rights for the partners.
- Consider the impact of these rules on the terms of partnership agreements as well as due diligence and negotiation strategies for future investments into pre-existing partnerships.
- Consider options available to fund and allocate the partnership tax liability.
- Address if partners are required to file amended returns and how compliance can be substantiated to reduce an imputed underpayment.
- Keep viable the option to elect-out of the BBA audit rules by restricting transfers of partnership interests to ineligible partners.
- Maintain a flexible partnership agreement in case the BBA rules change.
- Continue to monitor state conformity, if any.

Taking these action steps now — while there is still time to contemplate your options — should be carefully weighed, even though the statute may change in the interim.

Contact Us

For more information on the impact of the new partnership audit rules on your partnership, please contact Alan S. Kufeld, CPA, Partner at akufeld@pkfod.com or Leo Parmegiani, CPA, Partner at lparmegiani@pkfod.com or your PKF O'Connor Davies' tax advisor.

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