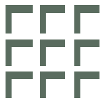

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# CHANGES TO IRS PARTNERSHIP AUDIT RULES

The Bipartisan Budget Act of 2015 (the Act) enacted late last year repeals the existing partnership audit rules known as the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) and will allow the IRS to collect taxes associated with audit adjustments at the partnership level, rather than passing adjustments through to the individual partners. Although the new law will not go into effect until January 1, 2018, partnerships and partners should start planning early to ensure their interests are protected, and rights and obligations are clearly understood by the current and former partners. A summary of the statutory revisions is as follows:

1. New tax terms and concepts created – In addition to replacing the term "tax matters partner' used under the TEFRA with a new term "partnership representative", the Act also creates other new terms and concepts such as "imputed underpayment", "adjustment year", and "reviewed year".

2. Entity-level tax imposed – The new law requires the IRS to assess and collect from the partnership an imputed underpayment in the year the audit is completed (the adjustment year) that is calculated using the highest tax rate for the year under audit (the reviewed year). In other words, the tax is imposed on the current partners, not the reviewed-year partners. To avoid this, partners may consider the following options:

   a. Elect out of the Act. This opt-out election is made annually on a timely-filed tax return, and is only available to partnerships with less than 100 partners and in which no partner is itself a partnership.

   b. Provide the IRS and the reviewed-year partners an adjustment statement detailing each reviewed-year partner's share of the adjustment assessed by the IRS, effectively shifting the tax liability to the reviewed-year partners' current year individual returns. This election must be made within 45 days after receipt of the IRS final adjustment.

   c. If one or more reviewed-year partners file amended returns for the reviewed year and pay the tax attributable to the IRS adjustment allocable to them, the imputed underpayment can be reduced. This information must be submitted to the IRS within 270 days following receipt of the IRS final adjustment.

3. Partnership representative (PR) – Under the Act, the PR has the sole authority to act on behalf of the partnership; the partnership and all partners are bound by actions taken by the PR. Additionally, the new rule restricts other partners' participation in an IRS examination or litigation with the IRS and if no PR is designated, the IRS has the authority to designate one.

To comply with the new law, we suggest partnerships and partners review and modify the indemnification and tax procedure provisions of the partnership agreements to incorporate new terms and concepts discussed above. Please do not hesitate to contact us if you have any questions regarding the Act or how its various provisions may impact your partnership. You may view a copy of this and other FBD memos on our website under PUBLICATIONS - [http://www.fbco.com/publications/Client memos](http://www.fbco.com/publications/Client memos).

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