Year-End Updates on Partnership Representatives

November 6, 2018

Summer 2018 proved to be an active time in the implementation cycle of the new partnership audit regime, created under the Bipartisan Budget Act of 2015 ("BBA"). As this is the first tax year in which the new regime will apply to partnership audits, the Internal Revenue Service ("IRS") issued a plethora of proposed and final regulations to assist taxpayers in navigating the audit process. ***Partnerships that have not yet reviewed their agreements, should take steps now to comply with the new rules and regulations***. With the year coming to a close, we at www.PartnershipRepresentative.com thought now would be a good time to update readers on the status of the new partnership audit rules and regulations.

I. Partnership Representative Regulations

One of the biggest changes to the partnership audit process was the creation of the partnership representative, the replacement for the Tax Matters Partner ("TMP") under the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") audit process. The new partnership representative will have the power to bind the partnership and all partners to any audit determinations. The IRS previously issued proposed regulations on the selection and powers of the partnership representative. After notice and comment on the proposed regulations, the IRS published final regulations in August 2018 (click here). The final regulations provide a great deal of flexibility as to who may be selected as a partnership's partnership representative. Unlike under TEFRA, which required a partner (or member in the limited liability company structure) to serve as the TMP, any individual or entity may be selected as the partnership representative. The individual or entity can come from entirely outside of the partnership. A partnership can even select itself as its own partnership representative. If an entity is chosen as the partnership representative, a "designated individual" must be selected from within the entity to work with the IRS in the event of a partnership audit. Additionally, the selected representative must have substantial presence in the United States ("U.S.") to serve as a partnership representative. Substantial presence requires the partnership representative to have a U.S. taxpayer identification number, telephone number, and postal address. Further, to satisfy the substantial presence requirement, the partnership representative must make themselves reasonably available to meet and communicate with the IRS (for a more thorough explanation of the partnership representative regulations, please see INSIGHT: People, Places, and Things: Final Regulations on the Eligibility, Designation, Revocation, and Authority of Partnership Representatives, *Bloomberg Tax: Daily Tax Report* (September 11, 2018)).

Generally, once a partnership representative is chosen for a particular tax year, the designation cannot be changed until the partnership receives notice of its selection for audit. The only way to change the designation prior to selection for audit is to file an administrative adjustment request ("AAR"); however, the filing of an AAR must be accompanied by some form of substantive change to the partnership's tax return. The AAR cannot be filed to just change the partnership representative. Otherwise, a partnership must wait until selection for audit to change the partnership representative. While this may seem like an unreasonable burden on partnerships, this is not likely to cause a problem. A partnership representative's power and responsibilities only go into effect once

the partnership is selected for audit. In the event a partnership does not feel comfortable with its previously selected partnership representative (i.e., a falling out with the partnership representative, or even the death of the partnership representative), the partnership will immediately be able to revoke the partnership representative's authority by filing a Form 8979, Partnership Representative Revocation, Designation, and Resignation Form. The IRS published a draft of the form in August 2018 (click here).

II. Proposed Regulations: Centralized Audit Regime

In August, the IRS issued new proposed regulations to address the other aspects of the BBA regime (click here). The new proposed regulations update previously published proposed regulations, to bring them in line with additional changes created to the audit process found in the Tax Technical Corrections Act of 2018. The proposed regulations mainly address updates to partnership-related items, imputed underpayments, and the administrative adjustment request process. Hearings on the proposed regulations were held in October, and we expect more guidance from the IRS in the near future.

III. Opting Out of the BBA Regime

Having previously published final regulations on elections out of the BBA partnership audit regime for eligible partnerships, this September, the IRS published draft instructions to Form 1065, Schedule B-2 (click here), addressing the process to opt out of the BBA regime. There are strict eligibility requirements to opt out of the regime, focusing on the number and type of partners in the partnership. Each eligible partnership should carefully consider whether it wishes to be bound by the BBA process, or rather, if it is better to opt out.

IV. Year-End Reminders

With the end of the year fast approaching, partnerships should start thinking about logical choices for who, or what, to select as its partnership representative. The designation is required on all future Forms 1065. Partnerships that still have not reviewed their partnership agreements in light of the new BBA regime should take proactive steps to ensure compliance with the new rules and regulations. Attorneys in Caplin & Drysdale's Tax Controversy Group are here to help with any partnership representative and partnership audit questions.

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