AICPA Asks Congress to Delay New IRS Partnership Audit Regime

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By Amy Hamilton

The American Institute of CPAs is asking Congress to delay for one year the effective date of the new centralized federal partnership audit regime, citing among its reasons the impact on state tax law.

Provisions of the new federal partnership audit regime generally took effect for tax years beginning after December 31, 2017.

But in a January 4 letter to leaders of the Senate Finance and House Ways and Means committees and to the acting IRS commissioner, the AICPA said Treasury and the IRS have not yet provided all necessary procedures and guidance for taxpayers to make informed decisions. The problem is compounded by the fact that the agencies now need to redirect significant resources to providing urgent guidance on the newly enacted federal tax reform bill, according to the AICPA.

Treasury and the IRS in June reissued proposed regulations (REG-136118-15) for the new partnership audit regime, and reserved several critical areas where guidance was planned for later release. Treasury has since issued proposed regulations addressing international tax rules (REG-119337-17) and addressing judicial review and the push-out election by tiered structures (REG-120232-17, REG-120233-17). Treasury also has issued final regulations (T.D. 9829) on electing out of the centralized partnership audit regime — but the AICPA said it is impossible for any partnership to meet the requirements to qualify for electing out for 2018.

The proposed regulations are likely to be revised, and temporary or final regulations in other critical reserved areas haven't been issued even though the provisions have taken effect, imposing undue burdens on taxpayers and the IRS, the AICPA said. Meanwhile, the new regime's impact on financial reporting standards remains unclear, and virtually every partnership operating in the United States will need to amend its partnership agreement to reflect provisions of the new audit regime, the letter said.

"Most states have no current provision allowing them to collect an audit assessment directly from a partnership operating within their borders," the AICPA added. "How the states are informed of the results of IRS audits under the new Regime, as well as what new policies and procedures they must enact into law to enable them to receive the correct additional state tax on their appropriate share of any adjustment, are two examples of the concerns facing every state tax department."

The letter referred to the development of model language for reporting federal partnership audit adjustments to the states under the new regime. A Multistate Tax Commission work group is holding meetings on the latest version of the draft developed by a task force that includes the American Bar Association Section of Taxation's State and Local Taxes Committee, the AICPA's state tax working group, the Council On State Taxation, the Tax Executives Institute, and the Institute for Professionals in Taxation.

“While I applaud the AICPA’s efforts, most of us tax practitioners aren’t very optimistic that Congress will take this up at this late date, since the rules are now effective and two new batches of implementing regulations were issued in the past few weeks,” said Bruce Ely of Bradley Arant Boult Cummings LLP in Birmingham, Alabama.

Ely, the former chair of the ABA SALT Committee task force, also provided observations about the proposed regulations allowing a tiered partnership to push adjustments beyond the first-tier partners.

Push-Out Rules

“Perhaps the most important issues we hope Treasury will address next are the treatment and calculation of capital accounts and basis adjustments, and we certainly hope to see those addressed in the next batch of proposed regs,” Ely said. Amendments to the basis adjustment rules included in the federal tax reform law must now be factored in, he added.

Ely said another unresolved issue, as practitioners see it, is whether a partnership representative (PR) must be appointed if his or her singular role is to check the box to elect the partnership out of the partnership audit rules.

“It’s a chicken-and-egg dilemma,” Ely said, adding that the AICPA first raised the issue. “Many if not most tax practitioners are playing it safe and recommending to all their subchapter K clients — large and small — that they appoint a PR, if only to have the appropriate person to check the opt-out box each year. Having a PR would also be crucial if the IRS rejects an opt-out election.”

Ely said both the final opt-out regulation and proposed push-out regs “contain a logistical nightmare” by requiring the partnership to acquire and update the names and proper taxpayer identification numbers of each shareholder of an S corporation partner, which is likely an even more difficult challenge with multitier partnership entities.

“We need more guidance — and some grace — on curative measures,” Ely said.

The authors of the final section 6221(b) regulation clarified that a partnership remains eligible to opt-out even if it has an S corporation partner that itself has shareholders who wouldn’t qualify as eligible partners. “It would have been disappointing had the authors taken the approach that if the S corp partner had even one [electing small business trust] or grantor trust or disregarded entity shareholder, that would prevent the partnership from opting out,” Ely said.

The comment period on the proposed push-out election by tiered structures is open until March 19.