PARTNERSHIP AUDIT RULES – FREQUENTLY ASKED QUESTIONS (FAQS) AND RESPONSES

Please be aware that the following responses to FAQ's are based upon the statutory legislation and related guidance in the form of enacted and proposed regulations existing as of October 16, 2018.

What are the new partnership audit rules?

In 2015, Congress passed new legislation to govern federal tax audits of partnerships and any ensuing litigation. Accordingly, for partnership tax years beginning after December 31, 2017, all audit, tax assessment, application of penalties or other additions are implemented at the partnership level. Likewise, only the partnership may petition for judicial review of any adjustments.

Under the new legislation, each partnership shall have a "partnership representative." This representative has the sole authority to act on behalf of the partnership, and both the partnership and the partners will be bound by those actions. Meaning, partners no longer have a legal right to receive notices or participate in the audit, appeals or any associated judicial review.

In addition to the legislative changes passed by Congress, the IRS has issued both final and proposed guidance on the new law in the form of regulations. These regulations along with the new legislation are commonly referred to as the new partnership audit rules.

Why were they implemented?

The new partnership audit rules are designed to make it easier for the IRS to examine partnerships and collect any resulting underpayments through the use of centralized proceedings.

Under the previous partnership audit rules, the audit, assessment and collection of tax was complex and administratively burdensome on the IRS. The need to identify and push adjustments through to each individual partner's returns was time consuming and difficult, particularly in the cases where partners were themselves flow-through entities. In addition, audit procedures frequently became more cumbersome and complex by the intervention of partners acting individually.

A 2013 government study concluded that these inefficiencies resulted in an extremely low rate of audits being completed in the partnership area. In addressing this, the report acknowledged that the IRS' ability to implement the recommended improvements was limited and that legislative action would be required.

Following this, Congress passed legislation to replace the existing statutes on partnership audits with the new partnership audit rules which enacted many of the legislative proposals from the report. At the time of enactment, Congress estimated that the changes would raise tax revenues of approximately $9.375 Billion over a period of ten years.

Given the background for the statutory changes, partnership audits are expected to increase significantly with respect to tax years for which the new rules are effective.

When are the new rules effective?

The new rules are generally effective for partnership audits of tax years beginning after December 31, 2017.

Under the new rules, certain designations and elections are required to be made in advance concurrent when filing the return rather than when the examination notice is received or later.

Each partnership is required to designate the "partnership representative" for that tax year on its original tax return beginning with the 2018 tax year.

Additionally, certain partnerships may qualify to elect out of the new rules. Partnerships that qualify and wish to make this election must do so with their timely filed tax return for the taxable year to which the election applies.

I heard some of the regulations are not final, why shouldn’t I wait until they are final before talking with my partners about this and starting to review my operating agreement?

While the IRS has previously stated its intention to finalize regulations by the end of the calendar year, they cannot do so prior to holding a public hearing and giving consideration to any electronic and written comments that are timely submitted to the IRS. The hearing date for the current version of proposed regulations was October 9th, which leaves very little time before year end for the IRS to give consideration, make any revisions and issue the regulations in final form. Additionally, the legislation passed by Congress will be effective beginning with 2018 tax years regardless of whether the IRS has issued guidance in the form of final regulations.

It is likely that taxpayers waiting to familiarize themselves with the new rules after the regulations are finalized may find themselves without enough time for the partner group to agree on important substantive issues and make any needed changes to their operating agreements prior to the date at which they must designate a representative or make certain elections. In the event of an audit, this may leave the partners vulnerable to unfavorable economic consequences with no avenue for recourse to be made whole.

My partnership is not under audit, do I really need to do anything about this prior to being notified of an audit?

Yes. Certain designations and elections relating to the new rules must be made with the timely filed tax return for each tax year.

In particular, the designation of the “partnership representative” must be made annually as part of the tax return filing. The new rules give the “partnership representative” the exclusive authority to bind the partnership and its partners in an audit, any subsequent appeal or judicial review. Unlike the current rules, the new law does not provide partners with any rights to be notified or to participate in the process and leaves partners with no ability to protest or appeal at the individual level. As a result, the primary method by which partners may retain the right to effectively participate in the process and to secure a remedy in the event the representative acts or fails to act in a certain manner may be through legal agreements such as the partnership operating agreement.

In light of this partnerships will need to take steps now to ensure any desired legal agreements are in place prior to designating a partnership representative.

Once final regulations are issued, partnerships will need to identify differences from the proposed regulations and determine what additional revisions, if any, may be needed.

Are all partnerships subject to these new rules?

Yes, the new rules apply to any partnership required to file a partnership tax return.

However, under the rules partnerships who meet certain eligibility requirements may elect not to apply the new partnership audit rules new audit regulations for that tax year.

Once made, the election for that year is binding on the partnership, all of its partners and any other person who has an interest in the partnership through one or more pass-through partners, and may not be revoked without the consent of the IRS.

Who can elect out?

Under the new rules, partnerships that have 100 or fewer partners where all partners are “eligible partners” may opt not to apply the new rules if the partnership makes a valid election with a timely filed tax return for such taxable year and meets the notification requirements.

How do you elect out?

Qualified partnerships who wish to elect out of the new rules may do so by affirmatively making the election on the partnership's timely filed tax return and including all of the information required by the IRS in regulations or any form, instructions or other guidance.

Under the regulations, partnerships must disclose to the IRS information about each person that was a partner at any time during the taxable year of the partnership, including each partner's:

- Name,
- Correct U.S. taxpayer identification number,
- Federal tax classification,
- An affirmative statement that the partner is an eligible partner under the regulations, and
- Any additional information required by the IRS on forms, instructions or other guidance.

In the case of partners who are S-corporations, the rules also require that the partnership disclose to the IRS the information above for each shareholder of the S corporation that was a shareholder at any time during the year.

A partnership must notify each of its partners of the election within 30 days of making the election.

Treasury has stated that the IRS intends to carefully review a partnership's decision to elect out of the new partnership audit rules.

In the event that the IRS determines that an election is invalid, the IRS will notify the taxpayer and the new partnership audit rules will apply to that year.

What are the rules for determining how many partners you have for purposes of making the election?

Under the new rules a partnership has 100 or fewer partners if it is required to furnish 100 or fewer K-1s, or equivalent statements under IRC 6013(b), for the taxable year.

The regulations also provide a special rule for making this determination in the case of partnerships having an S corporation as a partner. The partnership must take in to account each K-1 (or equivalent) statement required to be furnished by the S corporation partner to its shareholders for the S corporation's tax year ending with or within the partnership's tax year as if it were a K-1 statement required to be issued by the partnership in determining whether it meets the 100 partner limit. For example, assume ABC Partnership has 40 individual partners and 1 S corporation partner that has 60 shareholders. ABC Partnership would be considered to have 101 Schedule K-1s. Thus, it could not elect out of the new partnership audit rules.

It is important to note that under the rules a partnership who has only 100 or fewer partners at any given time during the year may still have more than 100 partners for purposes of meeting the eligibility requirements if mid-year ownership changes result in the partnership issuing more than 100 K-1s.

Treasury has indicated that the IRS will analyze whether an electing partnership has correctly identified all of its partners for federal income tax purposes. This analysis will include determining that the partnership has correctly identified its partners and will specifically give consideration as to whether two or more partnerships that have elected out should be recast under existing judicial doctrines and general federal tax principals as having formed one or more constructive or de facto partnerships for federal income tax purposes.

What happens if we elect out?

If a partnership elects out of the new rules, any audit, litigation, assessment and collection proceedings will be conducted at the partner level with each individual partner proceeding being subject to its own statute of limitations and venue.

Despite the fact that separate partner level proceedings for eligible electing partnerships results in a more burdensome audit and assessment process for the IRS, Treasury has stated that the IRS intends to increase the number of partnership audits for both partnerships that are subject to the new rules and those that have elected out.

Therefore, it is not anticipated that an election out of the new rules would reduce a partnership's likelihood of being audited.

What is an eligible partner for purposes of the election out?

An eligible partner means any partner that is an individual, a C corporation, a foreign entity that would be treated as a C corporation if it were a domestic entity under specifically identified regulations, an S corporation or an estate of a deceased partner.

The regulations also specify that a partner IS NOT an eligible partner if it is:

A. A partnership,

B. A trust,

C. A foreign entity that would NOT be treated as a C corporation if it were a domestic entity if the entity is classified as a per se corporation under reg. 301.7701-2(b)(1),(3),(4),(5),(6),(7) or (8) or is classified by default as a corporation under Reg 301.7701-3(b)(2)(i)(B) or is classified as a corporation in accordance with an election under Reg 301.7701-3(c),

D. A disregarded entity (examples - single member LLC, grantor trust),

E. An estate of an individual other than a deceased partner, or

F. Any person that holds an interest in the partnership on behalf of another person

Treasury has stated that the IRS intends to analyze whether the partnership has correctly identified all of its partners for federal income tax purposes and will be confirming that partners are not nominees or agents for the beneficial owner thereby making them an ineligible partner under item F above.

Are there reasons an eligible partnership wouldn't want to elect out?

Yes, the new partnership audit rules may be less administratively burdensome to taxpayers. If the partnership elects out, each partner will have to spend time responding to information documents requests and other audit issues individually rather than once at the partnership level.

Also, since the activities of the partnership are not audited separately from the activities of its partners electing out may allow the IRS to examine and adjust other partner level items that are not related to the partnership.

Are there reasons an eligible partnership that plans to elect out would need to review and revise their operating agreement?

Yes, partnerships that plan to elect out should still review and possibly revise their operating agreements in order to restrict certain actions which may cause the partnership to be ineligible for the election. Items for consideration include, but are not limited to, restricting transfers to ineligible partners, restricting transfers that would cause the partnership to issue more than 100 K-1s and restricting a partner from making an election to change its entity type that would result in it being an ineligible partner.

When considering these items, it is particularly important to remember that the list of ineligible partners includes certain entities that for all other tax purposes are disregarded such as single member LLC's and grantor trusts. It is not unusual for individuals to transfer assets to these types of entities to meet a non-tax need such as estate planning or legal protection of assets. Historically, there have generally been no tax consequences when this type of transfer occurs. As a result, if not legally restricted via the partnership agreement, these types of transfers would seem to pose a particular hazard with respect to the election as partners may engage in them without realizing it will have a tax related impact on the partnership and indirectly on themselves as partners.

Additionally, partnerships electing out should consider adding provisions to ensure that each partner timely provides the partnership with all of the information required to be reported to the IRS as part of each annual election. In particular, partnerships allowing S corporations as partners should make sure that the new provisions incorporate the requirement to provide all of the information to be reported with respect to the S corporation's shareholders as well.

In light of the fact that Treasury has stated the IRS will be carefully reviewing and analyzing a partnership's election out, partnerships should strongly consider making a protective designation of a partnership representative and including provisions in their operating agreement with respect to the representative's role in case the IRS determines that a partnership's election out is invalid.

What is a partnership representative?

The partnership representative is the person a partnership designates to be the sole point of contact with the IRS, the only person with authority to act on the partnership's behalf and whose actions, or lack thereof, are binding on both the partnership and its partners.

Since the representative is the only person who may represent the partnership in exams, agree or disagree with the IRS, make elections under the new rules, negotiate, settle, or bring a request for judicial review, careful selection of the representative and instituting appropriate checks and balances via the partnership operating agreement or other legal means are crucial to protecting the partnership and its partner.

Who is eligible to be the partnership representative?

The partnership representative does not have to be a partner. Any person with a substantial presence in the United States may act as the partnership representative.

For this purpose, a person is defined as being an individual, trust, estate, partnership, association, company or corporation. However, if a partnership designates an entity other than an individual as their partnership representative that designation will only be valid if the partnership also appoints an individual through whom the entity will act for all purposes under the audit rules, known as a designated individual. The designated individual must meet the substantial presence requirement and must be appointed at the same time the partnership representative is designated.

Under the rules in order to have a substantial presence in the United States (US) the person must –

- Be available to meet in person with the IRS in the US at a reasonable time and place, as is necessary and appropriate, as determined by the IRS;
- Have a street address that is in the US;
- Have a telephone number with a US area code where the person can be reached during normal business hours; and
- Have a US taxpayer identification number.

Can we designate DHG or one of its professionals as our partnership representative?

No, DHG or one of its professionals may not be designated as your partnership representative.

After giving careful consideration to the issue, we believe that to act as the designated partnership representative would not be in alignment with our mission of helping you, our clients, achieve their goals. We believe to act in this role would inhibit our relationship with you and have a negative impact on our ability to act as your personal advocate and trusted advisor. As such we believe that selection of a partnership representative other than DHG is more favorable for the partnership and its partners.

Due to the fact that each partner in a partnership will have their own unique tax attributes, it is likely that the partnership representative will be called upon to make decisions or otherwise take actions that will have disparate results among the partner group. If DHG or one of its professionals were to act as the partnership representative, it may result in a situation in which DHG had an obligation to act in a way that favors a non-client partner or that favors one client while posing a detriment to another client.

Beyond our concerns regarding serving you, our client, to the best of our ability, regulatory concerns also exist. In light of the fiduciary relationship created with the partnership and each of its partners, as well as the authoritative powers bestowed upon the designated partnership representative, we foresee that designation of DHG or one of its professionals as the partnership representative could create a conflict of interest under the following, which would not be able to be eliminated or reduced to an acceptable level through disclosure, consent or implementing other safeguards: AICPA Code of Conduct Section 1.100.020 Ethical Conflicts and Section 1.110.010 Conflicts of Interest for Members in Public Practice and Treasury Circular 230 section 10.29 Conflicts of Interest.

Lastly, we provide many services for our clients which require us to maintain independence under AICPA standards. Designation as the partnership representative would impair independence not only with respect to the partnership, but also with respect to any partner in the ownership chain.

Can my DHG professional still represent the partnership in an audit if they are not the designated partnership representative?

Yes, the rules specifically provide that the partnership representative can authorize a person to represent him in his capacity as the partnership representative before the IRS under a valid power of attorney.

This allows us to assist with a partnership examination, appeals or other proceeding by communicating with the IRS and advocating the partnership's position in a manner similar to what DHG would have done under the "old rules."

How is a partnership representative designated?

A partnership representative is designated for each tax year on the partnership tax return for the taxable year to which the designation applies. The designation must include all information required by forms, instructions or other guidance, including information about the designated individual if the designated representative is an entity (see FAQ on who is eligible to be the partnership representative).

The designation of a partnership representative, and designated individual if applicable, is effective only for the taxable year for which it is made.

Why would a partnership need or want to revise its operating agreement as a result of the new partnership audit rules?

The new rules are very complex and contain a myriad of options in the form of elections and modification requests. Failure to plan ahead and be prepared to make decisions within the timeframes required under the new rules may have a significant cost and produce inequitable results among the partner group. Additionally, under the new rules partners no longer have the opportunity to act independently and are bound by the actions of the new partnership representative. The new rules will have an economic impact on partners who enter and exit the partnership between the tax year being audited and the closing year of the exam; as a result this will likely be an area of concern in buy-sell transactions or upon admittance of new partners. For example, ABC Partnership is audited for its 2018 tax year, but the audit does not occur until 2020. In 2018, A, B, and C were the only partners. However, in 2020, A, B, and D were the only partners. Under the default rule of the new partnership audit rules, D would bear the tax implications for the 2018 audit, even though he was not a partner, because the partnership would be assessed the additional tax.

In order to minimize economic disparities, provide for an allowable amount of participation by the partner group, enact accountability for the partnership representative and ensure that information and decisions can be timely made, partnerships will want to review and potentially revise their operating agreements to address a number of items. Such items that might be considered include:

- How the partnership representative is chosen;
- Obligations and responsibilities of the partnership representative in making certain decisions and taking actions;
- Remedies for cases in which the partnership representative fails to operate within specified parameters;
- Level of due diligence required of the partnership representative in obtaining information to evaluate decisions;
- If and when an election out should be made in the case of an eligible partnership;
- Obligation of the partners to provide the information required to be reported as part of an election out within a prescribed timeframe;
- Restrictions on transfers that would result in the partnership being ineligible for the election out;
- Requirement that the partnership representative make certain elections or take certain actions based upon thresholds or parameters;
- Obligation of partners to provide specific tax information within a specific time so as to allow for modification requests ;
- Determination of when amended tax return filings by partners to obtain a modification would be required and obligation of all partners to file amended tax returns and provide a copy to the partnership representative within specified timeframes;
- Special allocations and/or capital call provisions with respect to partnership level tax liability assessed and other items such as adjustments that do not result in an imputed underpayment;
- Remedies in the case of partners who fail to cooperate within any of the agreed parameters; and
- Indemnification provisions relating to new and former partners.

What happens if the partnership does not designate a partnership representative?

If the partnership fails to designate a partnership representative the IRS will, upon determination that a designation is not in effect, notify the partnership (and the most recent partnership representative for that partnership tax year if one or more designations for the year were previously made and then revoked) that a partnership designation is not in effect.

The IRS will allow the partnership the opportunity to appoint an eligible representative within 30 days from the date of notification. If an eligible representative is not designated by the partnership within the required time period, the IRS will designate a partnership representative. The IRS may designate any person to be the partnership representative.

It is important to note that if the IRS received more than one revocation of a representative for the same taxable year signed by different persons within a 90 day period, the IRS may determine that a partnership representative has not been designated. In this particular instance, the partnership will not be given the opportunity to designate a representative prior to the IRS designating a person to be the partnership representative.

What happens if the designated partnership representative is determined to be ineligible?

If the designated partnership representative is ineligible, the IRS may determine that a designation is not in effect. In the event that the IRS determines a designation is not in effect due to ineligibility of the partnership representative, the IRS will notify the partnership and allow the partnership the opportunity to appoint an eligible successor representative within 30 days from the date of notification. If an eligible successor representative is not designated by the partnership within the required time period, the IRS may designate any person to be the partnership representative.

Unless and until the IRS makes a determination that a designation is not in effect, the action of the partnership representative is binding on the partnership. Therefore, any action previously taken by the partnership representative prior to this event continues to be binding on the partnership and its partners irrespective of the representative's ineligible status.

Can the partnership representative be changed?

The partnership may revoke its designation and appoint a different partnership representative only after receiving notice of an administrative proceeding from the IRS or with the filing of either an amended partnership tax return or Form 8082, Notice of Inconsistent Treatment or Administrative Adjustment Request (AAR).

However, the rules specifically prohibit the filing of an amended return or Form 8082 solely to change the designation of the partnership representative. Accordingly, the partnership representative may only be changed if there is either an error in the return requiring the filing of an amended partnership return or in the case of an audit.

The revocation notice must be provided to the IRS in writing and must contain specific information, appoint an eligible successor representative, be signed by the appropriate individual based on whether the partnership is a general partnership or a limited liability partnership, and be made in the form prescribed by the IRS through forms, instructions and other guidance. Failure to meet these requirements will result in the revocation being invalid and the original partnership representative continuing on as the designated partnership representative.

The partnership representative may also be changed in the event of a resignation by the individual designated as the representative. However, under the rules a partnership representative may only resign after the partnership has received a notice of an administrative proceeding from the IRS. In order to be effective, the partnership representative must notify the IRS of the resignation in writing and must meet certain rules regarding information and form of notification that are similar to the rules in place for a revocation.

Additionally, if the partnership representative was designated by the IRS rather than by the partnership that designation may only be revoked by the partnership if it obtains the permission of the IRS to do so. Likewise, a partnership representative who was designated by the IRS may only resign if permission to do so has been obtained from the IRS.

It is also important to note that the revocation is not effective until 30 days after the date the notice of revocation is sent to the IRS.

What is the default rule for calculating and assessing tax at the partnership level?

Generally at a high level, the default rule for calculating and assessing tax at the partnership level involves four steps. First, each adjustment is sorted into one of four types of groups and then further into subgroupings. Next, each subgrouping is netted to determine whether it results in an imputed underpayment. Subgroupings which do not result in an imputed underpayment, i.e. the tax effect of the net change is zero or is beneficial to the taxpayer, are then disregarded. Third, the net increase adjustment subgroupings, other than those in the credit group, are aggregated to arrive at the total netted partnership adjustment. Finally, this total netted partnership adjustment is multiplied by the highest rate of Federal income tax in effect for the reviewed year and increased or decreased by the net increase or decrease in credits resulting from partnership adjustments to arrive at the imputed underpayment.

The calculated imputed underpayment must be paid by the partnership in the same manner as if it were a tax imposed for the adjustment year.

Subgroupings that would not result in an imputed underpayment, and were therefore disregarded in arriving at the netted partnership adjustment, are taken into account by the partnership in the audit year as a K-1 reduction in non-separately stated income or as an increase or decrease in a separately stated item depending upon whether it is an item of income, gain, loss or deduction.

It is worth noting that special subgrouping rules apply to adjustments that reallocate the distributive share of an item from one or more partners to one or more other partners. Under these rules, adjustments increasing taxable income of partners will be included in one subgroup while the corresponding decreases to other partners are in a separate group. This will result in the partnership paying tax (and interest) on an adjustment that nets to zero across the partner group as a whole.

Are there ways to reduce the amount of tax calculated under the default rule?

Yes, there are a number of options available to the partnership representative under which they may be able to reduce the amount of tax calculated under the default rule. Some of these options include making a push-out election or requesting modifications in conjunction with providing supporting information to support such modification to the IRS within the prescribed time period. For example, a partnership can reduce or eliminate the amount of tax the partnership pays under the default rule by having partners amend their tax returns (or opt for the "pull-in" procedure) for the partner's share of the imputed underpayment. It is not required that all partners amend their returns or participate in the "pull-in" procedure. The "pull-in" procedure is an alternative to having partners file an amended return to reduce the imputed underpayment. Under the pull-in procedure, the partnership's imputed underpayment is reduced by the portion of the adjustments to partnership-related items that reviewed year partners take into account, supply all required information and timely pay the tax due.

The supporting information required will differ based upon the type of modification being requested, in some instances amended returns filed by relevant partners or information sufficient to file an amended return for relevant partners in conjunction with their agreement to adjust any tax attributes at the individual level may be required.

How could the partner group end up paying more tax and interest in total than might have been paid under the old rules?

If the taxes are assessed and paid at the partnership level under the default rule, generally the highest tax rate is used. Under the old rules the taxes were assessed and paid at the partner level based upon the individual partner's tax rate and tax attributes.

If the individual partners are in a lower tax bracket, more taxes will be paid at the partnership level than would have been paid at the individual partner level under the old rules. Additionally, under the general rule taxes assessed and paid at the partnership level do not take into consideration many of the tax attributes that may exist at the individual partner level. Examples include passive losses that are limited, losses suspended due to at risk and net operating loss carryforwards that could reduce the tax on any adjustments allocated to the partner.

How could a partner end up paying taxes that would otherwise have been the responsibility of another partner?

Under the default rule of the new rules, the partnership pays the income tax on the adjustment in the year the audit is concluded. As a result the partners in the partnership at the time of payment will be the partners to suffer the economic decrease due to the payment of taxes. Thus, if a partner acquires an interest in the partnership after the tax year(s) being audited but before the year the audit is settled, this new partner could incur the economic loss. Meanwhile, the old partner who sold his interest between the audit year(s) and the year of settlement will not be affected by the adjustment even though the old partner benefited initially. For example, ABC Partnership is audited for its 2018 tax year, but the audit does not occur until 2020. In 2018, A, B, and C were the only partners. However, in 2020, A, B, and D were the only partners. Under the default rule of the new partnership audit rules, D would bear the tax implications for the 2018 audit, even though he was not a partner, because the partnership would be assessed the additional tax.

Additionally, under the default rule, if the partnership agreement is not amended to specifically allocate the tax liability assessed at the partnership level or provide rules for how payment of the liability will be funded, some partners may end up effectively bearing more than their "true" share of the economic burden in instances where modification adjustments are made to reduce the liability calculated under the default rule. Some specific examples of scenarios in which this is likely to occur would include:

- When some but not all partners have favorable tax attributes that may be used to reduce the assessment;
- When some but not all partners file an amended return; or
- When some but not all partners provide information equivalent to amended return and agree to reduce their tax attributes at the individual level.

Is there any alternative to having the partnership pay the tax under the default rule?

A partnership may avoid paying tax on the imputed underpayment by electing to push this tax liability out to its partners. Alternatively, to reduce or eliminate the amount of tax the partnership pays under the default rule, the partnership agreement could be modified to require all partners to amend their tax returns (or opt for the "pull-in" procedure) for the partner's share of the imputed underpayment (or if the imputed underpayment exceeded a designated amount).

If the partnership representative so desires, an election can be made to "push out" the adjustments to the reviewed year partners of the partnership. Under the push out election, each partner who was a partner in the partnership for the tax year being audited will be responsible for paying the taxes attributable to that partner's share of the adjustment.

Under the push out election, the partners will be able to utilize any favorable tax attributes that exist at their individual level in determining the taxes due for their share of the adjustment. However, there is a trade-off for making the election in the form of an underpayment interest rate which is two percentage points higher than the rate which would apply under the default rule.

How is a push-out election made?

This election may only be made by the partnership representative and must be made within 45 days of the date the FPA (Final Partnership Adjustment) is made by the IRS. The time for filing such an election may not be extended.

The election must be signed by the partnership representative and specific statements must be provided to the reviewed year partners within 60 days of the date of the FPA. In addition, the election and statements must be filed in accordance with any forms, instructions and other guidance.

The statements to the reviewed year partners are required to include specific items of information, some of which will require the partnership to make additional calculations. Additionally, the partnership must provide separate statements to the partner for each reviewed year at issue and may not combine multiple years into a single statement.

Are there any reasons a partnership would not want to make a push-out election?

There are a number of reasons that a partnership may not want to make a push-out election, some of these include:

- The adjustment may be small and the administrative costs to comply with the reporting requirements under the election may be higher than the tax to be paid.
- The partner group may not have changed and the simplicity of paying at the partnership level may be desired.
- The partnership has a large number of partners with constant turnover and the administrative costs of keeping up with old partners' may not be cost effective or the partnership may not be able to fully complete the required statements for all partners within the prescribed 60 day period.
- The partnership may not want to incur the expense to prepare the statements for each partner regardless of the number of partners.
- The partner group has not changed and the amount of tax on the adjustments at the individual level is substantially similar to the tax amount under the default rule as a result the total paid by the partner group under the push out election may be greater due to the higher underpayment interest rate.
- The partner group has not changed and the amount of tax on adjustments at the individual level would be higher due to applicability of items such as alternative minimum tax (AMT), self-employment tax and the net investment tax at the individual partner level.