

# Insights

## Considerations for Business Owners as a Result of the New IRS Partnership Audit Rules

May 23, 2018

The Bipartisan Budget Act of 2015 (the "Act") changed the IRS partnership audit rules effective as of January 1, 2018. The changes to the partnership audit rules are unrelated to the much-publicized Tax Cuts and Jobs Act of 2017, but the new partnership audit rules should not be overlooked by partnerships when planning for 2018 and beyond.

The partnership audit rules govern IRS audits of partnerships, including LLCs treated as partnerships for federal tax purposes. For tax years ending before January 1, 2018, generally any taxes due as a result of an audit by the IRS on a partnership were imposed at the partner level, which meant that the partners during the year subject to the audit were responsible for any underpaid tax. However, under the new regime, instead of assessing an imputed tax underpayment amount at the partner level, the Act does so at the partnership level. This new system will make it easier for the IRS to audit partnerships, but it is a big change for the partnerships themselves. It also means that partners presently owning interests in the partnership are liable for the underpayment amounts, even for years prior to their admission as partners.

### **In light of the changes from the Act, partnerships need to consider the following:**

- 1. Appointing a Partnership Representative.** The Act eliminates the concept of the "Tax Matters Partner" and instead each partnership must appoint a "Partnership Representative" to serve as the sole individual or entity to act on behalf of the partnership in dealing with the IRS. The Act gives the Partnership Representative broad authority to bind the partnership (and the partners individually) in decisions with the IRS, including administrative or judicial actions. If no Partnership Representative is appointed by the partnership, the Act gives the IRS the power and authority to appoint anyone it chooses to serve as the Partnership Representative.
- 2. Electing out of the New Partnership Audit Rules.** Some partnerships have the ability to opt-out of the new partnership audit rules and would still be governed by the old rules. To be eligible for the opt-out, the partnership must have 100 or fewer partners and all partners must be "eligible partners" at all times during the tax year. Eligible partners include individuals, C corporations, certain foreign entities, S corporations (subject to special counting and disclosure rules), or an estate of a deceased partner. See Treas. Reg. 301.6221(b)-1. It is worthy to note that a single-member LLC is not an eligible partner, even where it is disregarded for federal income tax purposes from its individual owner.

These considerations and others may require changes to an entity's partnership agreement or operating agreement. For questions on how the changes to the partnership audit rules may impact your business, please contact Christopher Engel at [cengel@kdlegal.com](mailto:cengel@kdlegal.com) or your regular Krieg DeVault attorney.