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TaxNewsFlash

United States

No. 2018-113
March 23, 2018

Tax technical corrections are enacted, include partnership provisions

The president today signed legislation that includes tax technical correction provisions for certain partnership measures.

The legislation—**H.R. 1625** [PDF 3.27 MB] known as the "omnibus" appropriations bill—funds various government programs through the end of the fiscal year (i.e., through September 30, 2018). The bill was passed by the House on March 22, and by the Senate on March 23.

The technical corrections title of the bill does not include corrections relating to the new tax law (Pub. L. No. 115-97) as enacted on December 22, 2017. However, the technical corrections title does include technical corrections to legislation enacted before 2017—specifically changes to the partnership audit regime (including provisions to allow for the "push-out" of adjustments through passthrough partners in tiered structures).

Technical corrections concerning partnership audit regime

The omnibus appropriations legislation makes technical corrections to the partnership audit regime, including provisions to allow for the "push-out" of adjustments through passthrough partners in tiered structures (the "2018 Technical Corrections"). Technical corrections to the partnership audit provisions were proposed in December 2016—see **H.R. 6439** [PDF 284 KB] and **S. 3506** [PDF 416 KB]—(the "2016 Technical Corrections"). The 2018 Technical Corrections are substantially similar to the 2016 Technical Corrections, with some changes.

The 2018 Technical Corrections significantly clarify the scope of the regime, the calculation of an imputed underpayment, the process of modifying imputed underpayments and the alternative "push-out" payment mechanism of the push-out, as well as several additional clarifications regarding, among other things, the statutes of limitations and nonpayment of an imputed underpayment.

First, the 2018 Technical Corrections amend the scope of the provisions by changing the phrase, “income, gain, loss, deduction, or credit” and instead refer to partnership-related items, defined as any item or amount with respect to the partnership that is relevant in determining the income tax liability of any person, without regard to whether the item or amount appears on the partnership’s return and including an imputed underpayment and an item or amount relating to any transaction with, basis in, or liability of, the partnership. The explanation provided by the Joint Committee on Taxation (JCT)—**JCX-6-18**—states:

> *…these partnership audit rules are not narrower than the Tax Equity and Fiscal Responsibility Act of 1982 (“TEFRA”) partnership audit rules, but rather, are intended to have a scope sufficient to address those items described as partnership items, affected items, and computational items in the TEFRA context in Treasury Regulations sections 301.6231(a)(3), 301.6231(a)(5), and 301.6231(a)(6), as well as any other items meeting the statutory definition of a partnership-related item.*

The clarification extends to judicial review of a partnership adjustment. The court has jurisdiction to review all partnership-related items for the year to which the notice of final partnership adjustment relates; the allocation of items among the partners; and the application of penalties, additions to tax, and additional amounts.

Additionally, the Technical Corrections clarify that the partnership audit rules do not apply to taxes or require withholding under the self-employment tax or net investment income tax provisions, the nonresident alien and foreign corporation withholding provisions, or the FATCA withholding provisions (Code chapters 2, 2A, 3 and 4, respectively). However, to the extent relevant, a partnership adjustment regarding income tax is taken into account for purposes of determining the tax under these other chapters.

Push-out adjustments

The 2018 Technical Corrections contain welcome clarifications to the alternative payment mechanism under the new regime—the election to push out adjustments to partners under section 6226 rather than pay at the partnership level under section 6225. Specifically, the amended provision allows adjustments to be pushed out through the tiers in a tiered-partnership structure. As previously provided in the 2016 Technical Corrections, the amended provision allows a partnership or S corporation partner that receives a push-out statement to push out the adjustments to its reviewed-year partners or shareholders by filing with the Treasury Secretary a partnership adjustment tracking report, furnishing push-out statements to partners similar to those required of the audited partnership, and providing such information as is required by the IRS not later than the due date for the return for the tax year of the audited partnership. Proposed Treasury regulations issued in December 2017—read

TaxNewsFlash—had similarly allowed a push-out through the tiers, and set forth detailed requirements regarding information required to be included in the furnished statements. The 2018 Technical Corrections also provide authority to the IRS to prescribe rules for trusts that receive push-out statements. Proposed Treasury regulations treat trusts as partnerships for purposes of the push-out election with respect to tiered partnerships.

The 2018 Technical Corrections make another welcome change to the rules regarding the push-out election. As originally enacted, the provision required a partner receiving a push-out statement to take into account only **increases** to a partner's income tax, and not **decreases.** Under the 2018 Technical Corrections, an amendment to the push-out alternative allows a reviewed year partner to take into account both increases and decreases to the partner's income tax. As a result, it appears to be possible to claim a refund with respect to net favorable adjustments pushed out under section 6226.The amendment clarifies that in a push-out, the partner's tax for the tax year that includes the date of the statement is adjusted by the aggregate of the correction amounts, and not the adjustment amounts.

Default centralized collection mechanism

With regard to the default centralized collection mechanism under section 6225, the 2018 Technical Corrections also make notable amendments.

First, the 2018 Technical Corrections clarify that when netting adjustments to calculate an imputed underpayment under section 6225, the default centralized payment mechanism, adjustments must be first separately determined and netted appropriately within each category required to be taken into account separately. The JCT explanation provides, by way of example, that items of different character (capital or ordinary) are not netted together in determining an amount of an imputed underpayment. Furthermore, any limitations that could be applicable to direct or indirect partners are taken into account in determining the imputed underpayment. The JCT explanation illustrates this rule with an example that an adjustment that increases losses that may be subject to the passive loss limitation rules is not taken into account in computing the imputed underpayment, although the Secretary may provide otherwise if the partnership establishes that the partners are not subject to the passive loss limitation rules. The 2018 Technical Corrections also clarify that the procedures for modification under section 6225(c) are available even if the adjustments to partnership-related items did not result in an imputed underpayment.

Pull-in procedure

As previously included in the 2016 Technical Corrections, the 2018 Technical Corrections provide for an alternative procedure to modifying an imputed underpayment by filing amended returns, or a "pull-in" procedure.

The "pull-in" procedure allows the partnership to reduce the imputed underpayment to the extent that direct and indirect partners adjust their tax attributes and pay the tax that would be due as if they amended their returns and provide the IRS with information substantiating that the tax was correctly computed and paid. However, they would not file an amended return. As the JCT explanation explains, this alternative mechanism allows the benefit of an amendment without the "corollary effects on the partners' returns" other than adjusting the attributes for the effects of the adjustments in other tax years. Presumably, this allows the effect of an amendment without opening the partners' statutes of limitations.

Interest rate

The 2018 Technical Corrections add provisions that increase the interest rate to 5% on amounts owed upon a partnership's failure to pay an imputed underpayment within 10 days after the Secretary provides notice and demand for the payment. In addition, the partners can be assessed a tax equal to a partner's proportionate share of the owed amount, based on a partner's distributive share (with the aggregate liability of the partners not exceeding 100%). When a partner becomes liable for an amount, the liability of the partnership is reduced upon payment of the amount by the partner.

CFC partners

The 2018 Technical Corrections add provisions regarding the treatment of controlled foreign corporations (CFCs) and passive foreign investment companies (PFICs)—items that were not included in the 2016 Technical Corrections. The 2018 Technical Corrections generally treat each partner that is a U.S. shareholder, as defined in section 957 or 953(c)(1) (with respect to the CFC partner), and each partner with a QEF election (with respect to the PFIC partner) as a partner.

Partnership procedural provisions in 2018 Technical Corrections

Allowing deposits to suspend interest

The 2018 Technical Corrections add a new provision that clarifies that, before the due date for payment of the imputed underpayment, a partnership (or, in the case of a partner payment pursuant to an election under section 6226, a partner) may make a cash deposit to suspend the running of interest as provided under the present-law rules in section 6602. The deposit is not treated as a tax payment.

Assessment of imputed underpayment not subject to deficiency procedures

The 2018 Technical Corrections provide that if after the assessment, the partnership fails to pay the imputed underpayment, assessment and collection may be made against adjustment-year partners for their proportionate shares. The Secretary may assess the tax, interest, and penalties on the proportionate share of each adjustment-year partner without issuing a statutory notice of deficiency.

The 2018 Technical Corrections also clarify that the assessment of any imputed underpayment is not subject to the deficiency procedures, but can be assessed and collected after notice and demand for payment. Any imputed underpayment that is pushed out to a partnership partner or S corporation is also not subject to the deficiency procedures, but can be assessed after notice and demand.

Statute of limitations on assessment and refunds

The 2018 Technical Corrections provide that for purposes of amended returns and the pull-in procedures, tax relating to a reviewed-year partnership item and the effect of the adjustments on tax attributes may be determined and assessed without regard to the otherwise applicable period of limitations in section 6501 and 6511.

The Technical Corrections also provide that the period for making adjustments is not limited for making a redetermination of foreign tax expenses under section 905(c); does not expire before the date in section 6501(c)(8) for failing to notify the Secretary of certain foreign transfers or in section 6501(c)(10) with respect to failure to report listed transactions; and clarifies a reference to section 6501(e) for substantial omission of income to incorporate a reference to constructive dividends, not just to other omitted items.

The Technical Corrections provide regulatory authority for special enforcement similar to prior-law TEFRA audit rules. The Secretary may provide special rules relating to jeopardy assessments, criminal investigations, indirect methods of proof of income, foreign partners or partnerships, and other matters presenting special enforcement considerations.