



# TaxNewsFlash

## United States



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## KPMG report: Reminder about partnership reporting for tax year 2021

For tax year 2021 reporting, partnerships retain the option to choose whether to report under the traditional lag method or adopt the modified partnership reporting method as set forth in the proposed regulations (the "Proposed Reg Method"). The IRS has stated informally that the Proposed Reg Method will remain optional until the regulations are finalized, and the Form 1042 instructions make it clear that the decision is optional for all partnerships for the 2021 tax year.

As a reminder, partnerships that elect into the Proposed Reg Method of reporting will need to do the following:

- Determine that all withholding is done at the time of the actual or deemed distribution
- Deposit all withholding to the partner's Form 1042 account with the IRS for the year in which the income was earned by the partnership (i.e., deposit income earned by the partnership in 2021 to the partnership's 2021 account even if the income was not distributed to the partners until 2022)
- Report all income earned by the partnership in 2021 that is distributed on or prior to March 15, 2022, on 2021 Forms 1042-S by the March 15, 2022 reporting deadline (or by the April 14, 2022 extension date)
- Report income earned by the partnership in 2021 that is distributed after March 15, 2022 (included the deemed distributions that occur on the Form K-1 reporting date) on 2021 Forms 1042-S by the September 15, 2022 filing deadline
- For 2021 Forms 1042-S reporting actual and deemed distributions made after March 15, 2022 (i.e., forms using the September 15 deadline), determine that Box 7c is checked to avoid being automatically triggered for late filing penalties
- File for Form 1042 extensions if the partnership will be issuing K-1s after March 15, 2022
- Report all income earned by the partnership in 2021 on the partnership's 2021 Form 1042 (including actual and deemed distributions made during 2022)

All partnerships filing under the Proposed Reg Method need to consider having their returns reviewed for a determination that the forms are completed properly to minimize the risk of penalties.

### KPMG observation

Tax professionals have seen the IRS issue penalty notices to partnerships that reported during 2020 under the Proposed Reg Method—even when such partnerships were reporting properly in accordance with the proposed regulations and form instructions. While this appears to be a system glitch (one that the IRS is aware of), some are also seeing some penalty abatement requests being denied for partnerships that followed the Proposed Reg Method.

Therefore, partnerships that have not yet elected into the Proposed Reg Method may want to consider continuing to use the traditional lag method for the time being—at least until these IRS processing issues are resolved.

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### Tables prepared by KPMG LLP illustrating the methods

## What Stays the Same? Distribution in Year Earned

### Scenario 1: Partnership earns income in 2019 and distributes that income to partners during 2019

|              | Traditional Lag Method   | Prop. Reg. Method |
|--------------|--|-------------------|
| Payment Date | Date of actual distribution (2019)   |                   |
| Withholding  | Withhold on date of actual distribution (2019)   |                   |
| Deposits     | Deposit applied to 2019 Year   |                   |
| Reporting    | Report income on Form 1042-S for 2019 Year<br>Deadline: Mar 15, 2020 (Apr 14, 2020 with extension) |                   |

## Differences – Distribution After Year Earned

**Scenario 2: Partnership earns income in 2019 and distributes that income to partners between Jan 1, 2020, and Mar 15, 2020**

|              | Traditional Lag Method   | Prop. Reg. Method   |
|--------------|--|---|
| Payment Date | Date of actual distribution (2020)   |   |
| Withholding  | Withhold on date of actual distribution (2020)   |   |
| Deposits     | Deposit applied to 2020 Year   | Deposit applied to 2019 Year  |
| Reporting    | <ul style="list-style-type: none"> <li>Report income on Form 1042-S for 2020 Year</li> <li>Deadline: Mar 15, 2021 (Apr 14, 2021 with extension)</li> </ul> | <ul style="list-style-type: none"> <li>Report income on Form 1042-S for 2019 Year</li> <li>Deadline: Mar 15, 2020 (Apr 14, 2020 with extension)</li> </ul> <p><i>NOTE: Deadline is an entire year earlier</i></p> |

## Differences – Distribution After Year Earned

**Scenario 3: Partnership earns income in 2019 and distributes that income to partners between Mar 15, 2020, and Sept 15, 2020**

|              | Traditional Lag Method   | Prop. Reg. Method   |
|--------------|--|---|
| Payment Date | Date of actual distribution (2020)   |   |
| Withholding  | Withhold on date of actual distribution (2020)   |   |
| Deposits     | Deposit applied to 2020 Year   | Deposit applied to 2019 Year  |
| Reporting    | <ul style="list-style-type: none"> <li>Report income on Form 1042-S for 2020 Year</li> <li>Deadline: Mar 15, 2021 (Apr 14, 2021 with extension)</li> </ul> | <ul style="list-style-type: none"> <li>Report income on Form 1042-S for 2019 Year</li> <li>Deadline: Sept 15, 2020</li> <li>Check Box 7c</li> </ul> |



## Differences – Distribution After Year Earned

**Scenario 4: Partnership earns income in 2019 and does not distribute to partners prior to K-1 filing date**

|              | Traditional Lag Method  | Prop. Reg. Method   |
|--------------|---|---|
| Payment Date | Earlier of date K-1 is filed or Sept 15, 2020 Deadline (2020)   |   |
| Withholding  | Earlier of date K-1 is filed or Sept 15, 2020 Deadline (2020)   |   |
| Deposits     | Deposit applied to 2020 Year  | Deposit applied to 2019 Year  |
| Reporting    | <ul style="list-style-type: none"><li>• Report income on Form 1042-S for 2020 Year</li><li>• Deadline: Mar 15, 2021 (Apr 14, 2021 with extension)</li></ul> | <ul style="list-style-type: none"><li>• Report income on Form 1042-S for 2019 Year</li><li>• Deadline: Sept 15, 2020</li><li>• Check Box 7c</li></ul> |

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