



**STATEMENT OF
THE AMERICAN INSTITUTE OF CPAs
PRESENTED TO
INTERNAL REVENUE SERVICE
FOR THE PUBLIC HEARING
ON
THE CENTRALIZED PARTNERSHIP AUDIT REGIME
PROPOSED REGULATIONS
([REG-136118-15](#), DOCKET ID [IRS-2017-0009](#))
SEPTEMBER 18, 2017**

Good morning. My name is Sarah Allen-Anthony and I am a Tax Senior Manager at Crowe Horwath LLP. My testimony today is on behalf of the American Institute of CPAs (AICPA), the national professional accounting association representing more than 418,000 members in 143 countries. I am currently a member of the AICPA Partnership Tax Technical Resource Panel.

On August 14, 2017, the AICPA submitted written comments to the IRS on the proposed regulations. My testimony today focuses on our recommendations and concerns related to several areas of the proposed regulations marked “Reserved,” the process for designating the Partnership Representative and allowing an audited partnership access to the IRS Office of Appeals (Appeals).

Adjustments to Partner Capital Account and Basis

The Centralized Partnership Audit Regime (the Regime) significantly changes the way adjustments made by the IRS during an examination are accounted for by a partnership. A bedrock principle of partnership taxation is that all items of income and expense flow through to the partnership’s owners, including adjustments related to IRS audits. The Regime replaces this long-standing method with one where the default mechanism requires the partnership to pay any additional tax due, resulting in significant administrative and accounting complexities.

One of the main areas of increased complexity involves the effect of audit adjustments on each partner’s capital account and partnership basis. To simplify the process, we recommend that a partnership allocate audit adjustments which result in an imputed underpayment under sections 705(a)(1)(B) or (2)(B) in accordance with the partnership agreement of the reviewed year. We also suggest subjecting the audit adjustments to the existing “substantial economic effect” rules under section 704.

Audit Adjustments When Reviewed Partner Retains Partnership Interest

For the portion of the audit adjustment allocated to a reviewed year partner that retains their ownership interest in the adjustment year, we recommend, for simplicity, that the following two rules apply:

- 1) First, if the partnership elects to pay the imputed underpayment or the partner elects to pay the safe harbor amount, then make the net adjustments for the reviewed and intervening years to the partner’s capital account and basis in the adjustment year.
- 2) Second, if the partner elects to file amended returns or the partner recalculates their tax liability for the reviewed and intervening years following a “push-out” election, make the adjustments in the appropriate tax year and reflect it on each year’s amended return or recalculation worksheet.

Audit Adjustments When Reviewed Year Partner Disposed of Partnership Interest

Next, I would like to convey our proposals related to the portion of the audit adjustment allocated to the interest of a reviewed year partner that has disposed of their interest prior to the adjustment year:

- 1) If the partnership elects to pay the imputed underpayment or the partner elects to pay the safe harbor amount, then the net adjustments for the reviewed and intervening years are made to the adjustment year partner's capital account and basis in the adjustment year.
- 2) If the partner elects to file amended returns or the partner recalculates their tax liability for the reviewed and intervening years including the year of disposition, make the adjustments in the appropriate tax year and reflect them on each year's amended return or recalculation worksheet.

Additionally, we suggest that the effect of adjustments related to any intervening years between the disposition year and the adjustment year, as well as any carryover adjustment from the reviewed year partner, are taken into account by the adjustment year partner in the adjustment year.

In both situations, for adjustment year partners which acquired their interest in a taxable transaction, make any necessary revision to their 743(b) adjustment in the adjustment year.

When an audit adjustment is allocated to the interest of a reviewed year partner redeemed-out by the partnership, we suggest allocating the adjustment in accordance with the partnership agreement of the adjustment year as a section 734(b) adjustment in the adjustment year.

We further recommend that the additional tax paid, along with the interest and penalties imposed on the underpayment of tax, are allocated in the same manner as the associated adjustment.

Push-Out Election for Tiered Partnership Structures

Next, I would like to address permitting the use of the push-out election by tiered partnerships. We propose that the IRS establish procedures to allow for the push-out of audit adjustments through a tiered partnership structure.

In general, we discourage establishing any limitations on tiers, dollar amounts, number of partners, or other attributes because those limitations may result in the partners paying inappropriate amounts of tax. We believe that the framework we proposed in our August 14th letter would result in a system that is administrable for both the IRS and taxpayers while allowing for each partner to more accurately pay their appropriate share of taxes on any audit adjustments. The framework would also enable the IRS to collect the appropriate amount of additional tax without the inefficiencies experienced with the current TEFRA system.

We envision having an audited partnership electing to push-out any adjustment under section 6226 complete a Partnership Adjustment Report (PAR) and "Adjustment K-1s" within 60 days after the audit's final determination date. The PAR and Adjustment K-1s would mimic the existing Schedule K and partner specific Schedule K-1 regime used for original returns with additional information provided, as needed, to accurately report the results of an examination.

Upon receipt of an Adjustment K-1 from an audited partnership, a partnership-partner would have an option to file a PAR and related Adjustment K-1s with the IRS and their own partners within 60 days of the date shown on the Adjustment K-1 received by the partnership-partner. The same

process and 60-day deadline will apply to each upper-tier partnership electing to further push-out the adjustments.

We also recommend that an S corporation's partners follow a similar procedure to report the properly allocable portion of the adjustment to the IRS and its owners.

If a partnership-partner in a tiered structure fails to file its PAR with the IRS within the required timeframe, we propose that the IRS issue an assessment of tax in an amount equal to the safe harbor payment calculated under the proposed regulations. For purposes of this provision, any partner which is not an individual is treated as if they were an individual subject to chapter 1 tax.

We suggest making all PARs and Adjustment K-1s due no later than the extended due date of the audited partnership's tax return for the taxable year in which the Final Partnership Adjustment (FPA) is issued. We believe that placing an overall time limit on the process is preferable to establishing a maximum allowable number of tiers.

In order to facilitate the collection and tracking, through a tiered partnership, of PARs and Adjustment K-1s, we propose creating a centralized special processing unit within the IRS. We also suggest assigning a control number to each audit which is a reporting requirement on any documents submitted to the IRS or taxpayers.

We would also like to suggest that the IRS establish procedures for the electronic submission of Adjustment K-1s to partners, similar to existing rules for original Schedules K-1. It is critical that any Adjustment K-1 is issued and received by the partners as expeditiously as possible, particularly in tiered partnership structures, which will help ensure that the IRS collects the appropriate amount of tax as efficiently as possible.

Access to the IRS Office of Appeals

Next, I would like to address our concern that there is no reference in either the preamble or the proposed regulations to an audited partnership's right to challenge various determinations under the Regime with Appeals. The appeals process is a vital option for taxpayers to resolve an issue without having to go to Tax Court. We think that the final regulations should provide an explicit right to challenge the following actions or determinations by the IRS via the Appeals process:

- 1) A determination by the IRS that an election to opt out under section 6221 is invalid.
- 2) A denial by the IRS of a requested modification to an imputed underpayment amount.
- 3) A denial by the IRS of a partner-level defense raised by the partnership prior to issuance of a FPA.
- 4) The underlying adjustments to the partnership's return appearing on a Notice of Proposed Partnership Adjustment (NOPPA).
- 5) A determination by the IRS that a partnership has ceased to exist under section 6241.

Further, we propose allowing a partnership the right to appeal the determinations under sections 6221 and 6241 above within 60 days of receipt of the determination.

We also recommend that the IRS establish a single unified appeals process for a partnership to challenge both the underlying adjustments and any denial of requested modifications. The partnership's right to challenge the underlying adjustments and any denial of requested modification should expire on the later of the conclusion of the 270-day period following the mailing of a NOPPA (including any extensions of that period agreed to by the IRS) or 45 days after the IRS has either accepted or denied all properly submitted requests for modification of the imputed underpayment amount.

Partnership Representative Designation and Replacement Procedures

Finally, I would like to highlight several of our concerns and recommendations regarding the proposed regulations on the designation, resignation and revocation of a partnership representative:

- 1) First, we oppose the proposed procedures for appointing a "designated individual" to act on behalf of an "entity partnership representative." We believe that the entity partnership representative, not the partnership, should select the person who will act as their liaison with the IRS during an examination.
- 2) Second, we recommend allowing a partnership the ability to revoke and replace their partnership representative at any time and that a partnership representative should also have the ability to resign at any time. The IRS has established procedures for tracking Power of Attorney designations that they could modify to accommodate the necessary tracking. We have concerns that a previously designated partnership representative could discontinue their business relationship with the partnership, no longer qualify as an eligible person, become deceased, or become an adverse party in relation to the partnership.
- 3) Third, we oppose the provision that allows a resigning partnership representative to appoint their own successor. A partnership is required to grant substantial control and authority over their business matters to the partnership representative. Unless a partnership fails to appoint any person as required by the proposed regulations, they should maintain sole authority to appoint their partnership representative.
- 4) Finally, we recommend that the IRS clarify that all partnerships, even those electing to opt-out of the Regime under section 6221, are required to appoint a partnership representative on their timely filed tax return in order to protect the interests of both the IRS and the partnership itself.

The AICPA appreciates the opportunity to testify today. We hope Treasury and the IRS will consider these thoughts and our comment letter as you move forward in developing the final regulations, forms and procedures necessary to implement the Centralized Partnership Audit Regime.