Final Regulations of the Centralized Partnership Audit Regime (CPAR)

Summary of Treasury Decision 9844

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Overview

Effective date of Final Regulations: February 27, 2019

Applies to: Partnerships subject to the Centralized Partnership Audit Regime (CPAR) (generally taxable years beginning in 2018, unless partnership elected to apply the CPAR early).

Reminder: CPAR examination and adjustment is at the **partnership** level (subject to pull in and push out elections). Adjustment year partners may be liable for adjustment, even if they were not partners during the review year.

- **Pull in election:** Review year partners amend their returns in accordance with the imputed underpayment and pays their share of the adjustment (which reduces the adjustment at the partnership level). Partnership is still liable for partners that do not amend their returns.
- **Push out election:** Partnership makes an election that forces the review year partners to be liable. Partnership is responsible for determining each review year partner's liability. An additional 2% interest is applied.
- **Partnership Representative** – the Tax Matters Partner (times 1000). PR does not need to be a partner. IRS can pick the PR in certain circumstances (for example, if designated PR is not eligible).
    - June 21, 2019 TaxNotes article – IRS representative stated "the most important criteria for us is that it be a partner for the reviewed year, I think that's like a super favor because those are the ones most effected."

Pertinent Changes in Final Regulations

A substantial majority of the changes in the final regulations, when compared to the proposed regulations, are really clarifying revisions.

Changes discussed in this presentation:

1. Partner's Return Must be Consistent with Partnership Return
2. Determination of an Imputed Underpayment and Modification of an Imputed Underpayment
3. Election for alternative to payment of the imputed underpayment (the "Push-Out Election")
4. Interest and Penalties Related to Imputed Underpayments
5. Electing Out of CPAR

Part 1

PARTNER'S RETURN MUST BE CONSISTENT WITH PARTNERSHIP RETURN

Consistency Rule

The treatment of partnership-related items on a partner's return must be consistent with the treatment of such items on the partnership return in all respects, including the amount, timing, and characterization of such items

- Final Regulations clarify that "partner's return" includes **any return, statement, schedule, or list, and any amendment or supplement thereto**, filed by the partner with respect to any tax imposed by the Code

Inconsistent treatment is **permitted** in a specific circumstance: so long as a partner notifies the IRS of an inconsistent treatment, in the form and manner prescribed by the IRS, by attaching a statement to the partner's return (including an amended return) on which the partnership-related item is treated inconsistently, the consistency requirement and effect on inconsistent treatment do not apply to that partnership-related item.

§ 301.6222-1(a); § 301.6222-1(b)

Proceeding to Adjust an Identified, Inconsistently Reported Item

Final Rule: All partners, including partners that have filed notice of inconsistent treatment, are bound by the actions of the partnership and any final decision in a proceeding with respect to the partnership under the CPAR.

- This applies even if there is no proceeding with respect to the partner regarding the identified, inconsistently reported partnership-related item.
- The proposed regulations gave the IRS discretion to make the adjustment to the identified, inconsistently reported item.

§ 301.6222-1(c)(4)(i)

If the IRS withdraws a Notice of Administrative Proceeding (NAP) or Notice of Proposed Partnership Adjustment (NOPPA), then a partner may treat the an item inconsistently from how the item was treated on the partnership return. § 301.6231-1(f)

Part 2

DETERMINATION OF AN IMPUTED UNDERPAYMENT AND MODIFICATION OF AN IMPUTED UNDERPAYMENT

Credit Recapture

Final regulations provide that in general, the full amount of credit recapture is taken into account in determining a partnership's imputed underpayments, regardless of whether the partners actually benefitted from the recaptured credits.

The onus is on the partnership to affirmatively demonstrate to the satisfaction of the IRS during exam that the credit recapture should be taken into account differently pursuant to a modification request.

- This is in line with the CPAR, which determines the imputed underpayment at the partnership level (i.e., it does not look at the attributes of the partners).

Modification Procedure of an Imputed Underpayment

Partnership representative may request modification based on how adjusted items were taken into account by a partner prior to the item being adjusted by the IRS.

- § 301.6225-2(d)(2)(ii)
- Disregarded entities: a partnership may not request modification with respect to a direct or indirect partner that is a wholly-owned entity disregarded as separate from its owner for Federal income tax purposes
  - § 301.6225-2(a)
  - Note that a "disregarded entity" is not an "eligible partner" for purposes of electing out of the CPAR.

To request a modification, the partnership representative must furnish to the IRS information as required by forms, instructions, or other guidance prescribed by the IRS or as is otherwise requested by the IRS. The proposed regulations included an enumerated list of necessary items, so the final regulations provide additional flexibility.

- IRS will deny modification not only for the failure to substantiate a modification request but also for the failure to make any required payments during the time periods under § 301.6225-2.
- This indicates the partnership will be required to pay the adjustment before the IRS will approve a modification request.

Part 3

ELECTION FOR ALTERNATIVE TO PAYMENT OF THE IMPUTED UNDERPAYMENT (THE "PUSH-OUT ELECTION")

Notification that an Election Under 6226 Is Invalid

Background:

- When the partnership makes a push out election, it provides statements to its review year partners that includes certain items related to the partner (i.e., name, TIN, last known address, etc.) and the determination of the partner's share of adjustments.

Final regulation adds that the IRS may determine a push out election is invalid **without first notifying the partnership or providing the partnership an opportunity to correct any failures** to satisfy all the provisions of § 301.6226-1 and § 301.6226-2, including an opportunity to correct errors pursuant to § 301.6226-2(d) (i.e., the provision that allows the partnership to correct the statements provided to its partners).

- Explanation of provisions does provide, however, that the IRS intends to develop procedures under which the IRS will first contact the partnership prior to determining the push out election is invalid "in certain cases." The procedures, if adopted, will be set forth in future sub-regulatory guidance.

Corrections of Errors in Statements

Final regulations clarify that the IRS may not invalidate an election based on errors that are timely corrected by the partnership in accordance with § 301.6226-2(d)

- However, any errors in statements furnished by the partnership are subject to **penalty**
- If the IRS discovers or otherwise becomes aware of errors in statements, the IRS is under no obligation to require the partnership to provide additional information or to correct any errors, allowing the IRS to invalidate the election
- § 301.6226-2(d); § 301.6226-2(a)

Part 4

INTEREST IN PENALTIES RELATED TO IMPUTED UNDERPAYMENTS

Interest on Penalties, Additions to Tax, and Additional Amounts

- **Proposed**: provided that interest on any penalties, additions to tax, or additional amounts is calculated from the due date (**without extension**) of the reviewed year partner's return for the applicable taxable year until the amount is paid
  - § 301.6226-3(c)(2)
- **Final**: provides that interest on any penalties, additions to tax, or additional amounts is calculated from the due date (**including any extension**) of the reviewed year partner's return for the applicable tax year until the amount is paid
  - § 301.6226-3(c)(2)

Part 5

ELECTING OUT OF CPAR

§ 6221 of the Internal Revenue Code

- **§ 6221(b)**: provides that certain partnerships may elect out of the CPAR
  - Eligibility to elect out of the CPAR turns on whether the following requirements are met:
    - The partnership has 100 or fewer partners for the taxable year
    - Each partner in the partnership is an eligible partner
    - The election is timely made in the manner prescribed by the Secretary, and
    - The partnership notifies its partners of the election in the manner prescribed by the Secretary

§ 6221(b) Requirements Explained

- The partnership has 100 or fewer partners for the taxable year
  - Number of partners is determined by counting the number of statements required to be furnished by the partnership under § 6031(b) and the number of statements required to be furnished by any S corporation partners of the partnership
- Each partner in the partnership is an eligible partner
  - An *eligible* partner is a(n): partner that is an individual, C corporation, eligible foreign entity, S corporation, or estate of a deceased partner
  - A *non-eligible* partner is a(n): partnership, trust, foreign entity that is not an eligible foreign entity, *disregarded entity*, nominee or other similar person that holds an interest on behalf of another person, or estate of an individual other than a deceased partner

Special Enforcement Concerns – QSubs

- **Enforcement concerns arise in situations where a QSub is a partner in a partnership (Notice 2019-06)**
  - Future regulations will provide that § 6221(b) (the provision that allows a partnership to elect out of CPAR) generally does not apply to a partnership with a QSub as a partner, unless an exception is met (exceptions TBD)
    - Concern is that the partnership would have more than 100 ultimate partners and still be eligible to elect out.