[JOINT COMMITTEE PRINT]

GENERAL EXPLANATION OF TAX LEGISLATION ENACTED IN 2015

PREPARED BY THE STAFF

OF THE

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- 85 percent to 115 percent for 2021,
- 80 percent to 120 percent for 2022,
- 75 percent to 125 percent for 2023, and
- 70 percent to 130 percent for 2024 or later.

In addition, for purposes of the additional information that must be provided in a funding notice for an applicable plan year, an applicable plan year includes any plan year that begins after December 31, 2011, and before January 1, 2023, and that otherwise meets the definition of applicable plan year.

Effective Date

The provision applies to plan years beginning after December 31, 2015.

TITLE XI—REVENUE PROVISIONS RELATED TO TAX COMPLIANCE

A. Partnership Audits and Adjustments (sec. 1101 of the Act and secs. 6221–6241 of the Code)

Present Law

Reporting requirements of partnerships generally

For Federal income tax purposes, a partnership is not a taxable entity. Instead, a partnership is a conduit and the items of partnership income, deduction, gain, loss, and credit are taken into account on the partners' income tax returns. A partnership is required to file an annual information return setting forth items of partnership information necessary to carry out the income tax (Form 1065).[168] A partnership is also required to furnish to each partner a statement of such partnership information as is relevant to the partner's income tax (Schedule K–1).[169] For taxable years beginning after December 31, 2015, partnership returns and partner statements are generally due by the 15th day of the third month after the end of the partnership taxable year.[170]

Rules relating to audit and adjustment procedures for partnerships

There are three sets of rules for tax audits and adjustments for partners and partnerships. First, for partnerships with more than 100 partners and that so elect, the electing large partnership rules enacted in 1997 apply.[171] Relatively few partnerships have made this election. Second, for partnerships with more than 10 partners or with passthroughs as partners (and that are not electing large partnerships), the TEFRA rules enacted in 1982 apply.[172] Under these two sets of rules, partnership items generally are determined at the partnership level under unified procedures. Third, for part-

[168] Sec. 6031(a).
[169] Sec. 6031(b).
[170] See sec. 6072(b) as amended by Pub. L. No. 114–41, sec. 2006 (114th Congress). For taxable years beginning after December 31, 2015, a partnership can request a six-month extension of time to file. See also Department of the Treasury, Internal Revenue Service, *2011 Instructions for Form 1065, U.S. Return of Partnership Income*, p. 4.
[171] Secs. 6240–6255.
[172] Secs. 6221–6234. TEFRA refers to the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. No. 97–248), in which these rules were enacted.

nerships with 10 or fewer partners that have not elected the TEFRA audit rules, audit and adjustment rules applicable generally to taxpayers subject to the Federal income tax apply.[173]

For a partnership with few partners that does not elect to be governed by TEFRA rules, the tax treatment of an adjustment to a partnership's items of income, gain, loss, deduction, or credit is determined for each partner in separate proceedings, both administrative and judicial. These are known as deficiency proceedings. Adjustments to items of income, gains, losses, deductions, or credits of the partnership generally are made in separate actions for each partner. Particularly in the case of a partnership with partners in different locations, this may result in separate judicial determinations in different courts that are potentially subject to different appellate jurisdiction. Prior to the 1982 enactment of TEFRA, these had been the rules for all adjustments with respect to partners, regardless of the number of partners in the partnership.

TEFRA rules

Unified rules

TEFRA established unified rules. These rules require the tax treatment of all "partnership items" to be determined at the partnership, rather than the partner, level. Partnership items are those items that are more appropriately determined at the partnership level than at the partner level, as provided by regulations.[174] The IRS may challenge the reporting position of a partnership by conducting a single administrative proceeding to resolve issues with respect to all partners.

The rationale stated in 1982 for adding new rules for partnerships was that "[d]etermination of the tax liability of partners resulted in administrative problems under prior law due to the fragmented nature of such determinations. These problems became excessively burdensome as partnership syndications have developed and grown in recent years. Large partnerships with partners in many audit jurisdictions result in the statute of limitations expiring with respect to some partners while other partners are required to pay additional taxes. Where there are tiered partnerships, identifying the taxpayer is difficult."[175]

The TEFRA rules do not, however, change the process for collecting underpayments with respect to deficiencies at the partner (not the partnership) level, though a settlement agreement with respect to partnership items binds all parties to the settlement.[176]

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[173] Secs. 6231 and 6201 *et seq*.

[174] Sec. 6231(a)(3). Any item that is affected by a partnership item (for example, on the partner's return) is an "affected item." Affected items of a partner are subject to determination at the partner level. Sec. 6231(a)(5).

[175] See Joint Committee on Taxation, *General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982* (JCS–38–82), December 31, 1982, p. 268. Additional reasons for the 1982 change mentioned include the problems of duplication of administrative and judicial effort, inconsistent results, difficulty of reaching settlement, and inadequacy of prior-law filing and recordkeeping requirements for foreign partnerships with U.S. partners.

[176] Sec. 6224(c). The IRS has set forth procedures for entering into such partnership audit settlement agreements, which are summarized in Part F of Chief Counsel Notice 2009–27, "Frequently Asked Questions Regarding The Unified Partnership Audit And Litigation Procedures Set Forth In Sections 6221–6234," IRS CC Notice 2009–027, August 21, 2009.

Tax Matters Partner

The TEFRA rules establish the Tax Matters Partner as the primary representative of a partnership in dealings with the IRS. The Tax Matters Partner is a general partner designated by the partnership or, in the absence of designation, the general partner with the largest profits interest at the close of the taxable year. If no Tax Matters Partner is designated, and it is impractical to apply the largest profits interest rule, the IRS may select any partner as the Tax Matters Partner.

Notice requirements: notice required to partners separately

The IRS generally is required to give notice of the beginning of partnership-level administrative proceedings and any resulting administrative adjustment to all partners whose names and addresses are furnished to the IRS. For partnerships with more than 100 partners, however, the IRS generally is not required to give notice to any partner whose profits interest is less than one percent.

Partners must report items consistently with the partnership

Partners are required to report partnership items consistently with the partnership's reporting, unless the partner notifies the IRS of inconsistent treatment. If a partner fails to notify the IRS of inconsistent treatment, the IRS can assess that partner under its math error authority. That is, the IRS may make a computational adjustment and immediately assess any additional tax that results.[177] Additional tax attributable to an adjustment of a partnership item is assessed against each of the taxpayers who were partners in the year in which the understatement of tax liability arose.

Partners' limited ability to challenge partnership treatment

Partners have rights to participate in administrative proceedings at the partnership level, and can request an administrative adjustment or a refund for the partner's own separate tax liability. To the extent that a settlement is reached with respect to partnership items, all partners are entitled to consistent treatment.[178]

Statute of limitations

Absent an agreement to extend the statute of limitations, the IRS generally cannot adjust a partnership item for a partnership taxable year if more than three years have elapsed since the later of the filing of the partnership return, or the last day for the filing of the partnership return (without extensions). The statute of limitations is extended in specified circumstances such as in the case of a false return, a substantial omission of income, or no return.

One-year period

If the administrative adjustment is timely made within the limitations period described above, the tax resulting from that adjustment, as well as the tax attributable to affected items, including related penalties or additions to tax, must be timely assessed. The

[177] Secs. 6222 and 6230(b).
[178] Sec. 6224.

period in which the tax must be assessed against the partners does not expire before one year following the date on which the final partnership administrative adjustment may no longer be petitioned to the U.S. Tax Court or, if a petition was filed, a decision of the court with respect to such petition is final.[179]

Adjudication of disputes concerning partnership items

After the IRS makes an administrative adjustment, the Tax Matters Partner (and, in limited circumstances, certain other partners) may file a petition for readjustment of partnership items in the Tax Court, the district court in which the partnership's principal place of business is located, or the Court of Federal Claims.

Electing large partnership audit rules

Definition of electing large partnership

In 1997, an additional audit system was enacted for electing large partnerships.[180] The 1997 legislation also enacted specific simplified reporting rules for electing large partnerships.[181] The provisions define an electing large partnership as any partnership that elects to be subject to the specified reporting and audit rules, if the number of partners in the partnership's preceding taxable year is 100 or more.[182]

The rationale stated in 1997 for adding new audit rules for large partnerships was that "[a]udit procedures for large partnerships are inefficient and more complex than those for other large entities. The IRS must assess any deficiency arising from a partnership audit against a large number of partners, many of whom cannot easily be located and some of whom are no longer partners. In addition, audit procedures are cumbersome and can be complicated further by the intervention of partners acting individually." [183]

Unified rules

As under the TEFRA partnership rules, electing large partnerships and their partners are subject to unified audit rules. Thus, the tax treatment of partnership items is determined at the partnership, rather than the partner, level.

Partnership representative

Each electing large partnership is required to designate a partner or other person to act on its behalf. If an electing large partnership fails to designate such a person, the IRS is permitted to designate any one of the partners as the person authorized to act on the partnership's behalf.

Notice requirements: separate partner notices not required

Unlike the TEFRA partnership audit rules, the IRS is not required to give notice to individual partners of the commencement of an administrative proceeding or of a final adjustment. Instead,

[179] Sec. 6229(d) and (g).
[180] Secs. 6240–6255, enacted by the Taxpayer Relief Act of 1997, Pub. L. No. 105–34.
[181] Secs. 771–777.
[182] Sec. 775.
[183] See Joint Committee on Taxation, *General Explanation of Tax Legislation Enacted in 1997* (JCS–23–97), December 17, 1997, p. 363.

the IRS is authorized to send notice of a partnership adjustment to the partnership itself by certified or registered mail. The IRS may give proper notice by mailing the notice to the last known address of the partnership, even if the partnership had terminated its existence.

Partners must report items consistently with the partnership

Under the electing large partnership audit rules, a partner is not permitted to report any partnership items inconsistently with the partnership return, even if the partner notifies the IRS of the inconsistency. The IRS may adjust a partnership item that was reported inconsistently by a partner and immediately assess any additional tax without first auditing the partnership.[184]

Adjustments flow through to persons that are partners in the year in which the adjustment takes effect

Unlike the TEFRA partnership audit rules, however, partnership adjustments generally flow through to the partners for the year in which the adjustment takes effect.[185] Thus, the current-year partners' share of current-year partnership items of income, gains, losses, deductions, or credits are adjusted to reflect partnership adjustments that take effect in that year. The adjustments generally do not affect prior-year returns of any partners (except in the case of changes to any partner's distributive shares).

Partnership's payment of imputed underpayment is permitted

In lieu of passing through an adjustment to its partners, the partnership may elect to pay an imputed underpayment. The imputed underpayment generally is calculated by netting the adjustments to the income, gain, loss, or deductions of the partnership and multiplying that amount by the highest Federal income tax rate (whether individual or corporate). Adjustments to credits are taken into account as increases or decreases in the amount of tax. A partner may not file a claim for credit or refund of his allocable share of the payment. A partnership may make this election only if it meets requirements set forth in Treasury regulations designed to ensure payment (for example, in the case of a foreign partnership).

Regardless of whether a partnership adjustment passes through to the partners, an adjustment must be offset if it requires another adjustment in a year that is after the adjusted year and before the year the adjustment that was made takes effect.

For example, assume that an electing large partnership expenses a $1,000 item in year one. However, on audit in year four, it is determined that the item should have been capitalized and amortized ratably over 10 years rather than deducted in full in year one. The $900 adjustment for the improper deduction ($1,000 minus the year one amortization of $100) is offset by $100 of adjustments for amortization deductions in each of years two and three. The adjustment in year four is $700 (that is, $1,000 minus $300, the sum of the first three years' ratable amortization of $100 per year), apart

[184] Sec. 6241(b).
[185] Sec. 6242.

from any interest or penalty. The year four partners are required to include an additional $700 in income for that year. The partnership ratably amortizes the $700 in years four to 10.

Partnership, not partners separately, is liable for any penalties and interest

The partnership, rather than the partners individually, generally is liable for any interest and penalties that result from a partnership adjustment. Interest is computed for the period beginning on the return due date for the adjusted year and ending on the earlier of the return due date for the partnership taxable year in which the adjustment takes effect or the date the partnership pays the imputed underpayment. Thus, in the above example, the partnership is liable for four years' worth of interest (on a declining principal amount).

Penalties (such as the accuracy and fraud penalties) are determined on a year-by-year basis (without offsets) based on an imputed underpayment. All accuracy penalty criteria and waiver criteria (such as reasonable cause or substantial authority) are determined as if the partnership were a taxable individual. Accuracy and fraud penalties are assessed and accrue interest in the same manner as if asserted against a taxable individual.

Any payment (for Federal income taxes, interest, or penalties) that an electing large partnership is required to make is nondeductible.

If a partnership ceases to exist before a partnership adjustment takes effect, the former partners are required to take the adjustment into account, as provided by regulations. Regulations are also authorized to prevent abuse and to enforce efficiently the audit rules in circumstances that present special enforcement considerations (such as partnership bankruptcy).

Partners cannot request refunds separately

The IRS may challenge the reporting position of a partnership by conducting a single administrative proceeding to resolve the issue with respect to all partners. Unlike the TEFRA partnership audit rules, however, partners have no right individually to participate in settlement conferences or to request a refund.

Timing of Schedules K–1 to partners

An electing large partnership is required to furnish copies of information returns (Schedule K–1, Partner's Share of Income, Deductions, Credits, etc.) to partners by March 15 following the close of the partnership's taxable year (often a calendar year).[186]

Statute of limitations

Absent an agreement to extend the statute of limitations, the IRS generally cannot adjust a partnership item for a partnership taxable year if more than three years have elapsed since the later of the filing of the partnership return or the last day for the filing of the partnership return. The statute of limitations is extended in

[186] Sec. 6031(b).

specified circumstances such as in the case of a false return, a substantial omission of income, or no return.

Adjudication of disputes concerning partnership items

As under the TEFRA rules, a partnership adjustment can be challenged in the Tax Court, the district court in which the partnership's principal place of business is located, or the Court of Federal Claims. However, only the partnership, and not partners individually, can petition for a readjustment of partnership items.

If a petition for readjustment of partnership items is filed by the partnership, the court with which the petition is filed has jurisdiction to determine the tax treatment of all partnership items of the partnership for the partnership taxable year to which the notice of partnership adjustment relates, and the proper allocation of such items among the partners. Thus, the court's jurisdiction is not limited to the items adjusted in the notice.

Explanation of Provision

Repeal of TEFRA and electing large partnership rules

Generally for returns filed for partnership taxable years beginning after 2017, the provision repeals the tax reporting provisions and voluntary centralized audit procedures for electing large partnerships, as well as the TEFRA partnership audit and adjustment rules. In place of the repealed procedures, a centralized system for audit, adjustment, assessment, and collection of tax applies to all partnerships, except those eligible partnerships that have filed a valid election out. Electing out of the centralized system leaves applicable the present-law rules for deficiency proceedings. The centralized system is located in subchapter C of chapter 63 of the Code.

In General

Determination at partnership level

Under the centralized system, the audit of a partnership takes place at the partnership level. Any adjustment to items of income, gain, loss, deduction, or credit of a partnership for a partnership taxable year, and any partner's distributive share thereof, generally are determined at the partnership level.[187] Any tax attributable to these items generally is assessed and collected at the partnership level. The applicability of any penalty, addition to tax, or additional amount that relates to an adjustment of any item of income, gain, loss, deduction, or credit of a partnership for a partnership taxable year or to any partner's distributive share thereof is determined at the partnership level. Unlike prior law, distinctions between partnership items and affected items are no longer made. An underpayment of tax determined as a result of an examination of a taxable year is imputed to the year during which the adjustment is finally determined, and generally is assessed against and collected from the partnership with respect to that year rather than the reviewed year.

[187] Sec. 6221(a).

Under the centralized system, a partnership may seek modification of the imputed underpayment amount by providing the Secretary with specified information about the tax status of partners and about the nature and amount of items of income or gain, by means of reviewed-year partners filing amended returns with payment, or on the basis of other factors in regulations or guidance. A partnership may elect an alternative to partnership payment of the imputed underpayment in which each reviewed-year partner is furnished a statement of the partner's share of the adjustments (similar to Schedule K–1) and each such reviewed-year partner increases its tax for the year the statement is furnished. A partnership may file an administrative adjustment request.

Rules are provided relating to statutes of limitation and other applicable time periods, interest and penalties, judicial review, and other aspects of the centralized system under the provision.

Election out

The centralized system is applicable to any partnership unless it meets eligibility requirements and has made a valid election out for a taxable year.[188]

100 or fewer statements

A partnership may elect out of the centralized system (and it and its partners are governed by the present-law deficiency proceedings) for a partnership taxable year if it meets eligibility requirements. One of the eligibility requirements is that for the taxable year, the partnership is required to furnish 100 or fewer statements under section 6031(b) (Schedules K–1) with respect to its partners.

A further eligibility requirement for a partnership to make the election is that each of its partners is an individual, a deceased partner's estate, a C corporation, a foreign entity that would be required to be treated as a C corporation if it were a domestic entity, or an S corporation (provided special rules are met). A partnership with a foreign entity as a partner can meet this eligibility requirement if, under the rules of section 7701, the foreign entity would be taxable as a C corporation if it were domestic; that is, the foreign entity has elected to be, or is, treated as a per se corporation under the check-the-box regulatory rules under section 7701.[189] A C corporation partner that is a regulated investment company ("RIC") or a real estate investment trust ("REIT") does not prevent the partnership from being able to elect out, provided the applicable requirements are met.

Example

For example, a partnership is formed to conduct a joint venture between two corporations, X and Y. X's domestic C corporation subsidiary, W, owns a 50-percent interest in the partnership, and Y's domestic C corporation subsidiary, Z, owns a 50-percent interest in the partnership. The partnership is required to furnish two statements (Schedules K–1), one to W and one to Z. The partnership is

[188] Sec. 6221(b).
[189] See Treas. Reg. sec. 301.7701–2 and –3.

eligible to elect out of the centralized system for the taxable year, provided that the partnership meets the requirements (described below) as to the time and manner of electing out, including (among other requirements) disclosing to the Secretary the names and employer identification numbers of W and Z.

Time and manner of election out

The election is to be made with a timely-filed return of the partnership taxable year to which the election relates; the election is valid only for that year. The election must include the name and taxpayer identification number of each partner of the partnership in the manner prescribed by the Secretary. The partnership must notify each of its partners of the election in the manner prescribed by the Secretary.

S corporation partners

For a partnership with a partner that is an S corporation to elect out, the partnership is required to include with its election (in the manner prescribed by the Secretary) a disclosure of the name and taxpayer identification number of each person with respect to whom the S corporation must furnish a statement under section 6037(b) for the S corporation's taxable year ending with or within the partnership's taxable year for which the election is made. This requirement is met if the partnership discloses the name and taxpayer identification number of each S corporation shareholder with respect to which a statement (Schedule K–1) is required to be furnished under section 6037(b). These statements required to be furnished by the S corporation are treated as statements required to be furnished by the partnership for purposes of the 100-or-fewer-statements criterion for the partnership's eligibility to elect out.

Example

For example, if a partnership has 50 partners, 49 of which are individuals and one of which is an S corporation with 30 shareholders all of whom are individuals, the partnership is treated as being required to furnish 80 statements. This is the sum of 49 statements for individual partners, one statement for the S corporation partner, and 30 statements for individuals with respect to whom the S corporation must furnish statements. The partnership meets the 100-or-fewer-statements criterion for the partnership's eligibility to elect out.

Foreign partners

The Secretary may provide for an alternative form of identification of any foreign partners (for example, if the foreign partners do not have U.S. taxpayer identification numbers) for purposes of the requirement of disclosure of the name and taxpayer identification number of each partner by the partnership.

Other persons as partners

The Secretary may by regulation or other guidance identify other types of partners to whom rules similar to the special rules in the case of a partner that is an S corporation can apply. This guidance shall take into account, for purposes of applying the 100-or-fewer-

statements criterion,[190] each direct and indirect interest in the partnership of any person to which a statement (comparable to the partner statement under section 6031(b)) is required to be furnished by any person. Such guidance may also take into account any person with respect to which a comparable statement is not required to be furnished but which has an interest (direct or indirect) in the partnership. Further, such guidance shall require the partnership to disclose to the Secretary the name and taxpayer identification number of each person with respect to which a statement (comparable to the partner statement under section 6031(b)) is required to be furnished and of other persons with an interest (direct or indirect) in the partnership.

Examples

For example, assume that a partner of a partnership is a disregarded entity such as a State-law limited liability company ("LLC") with only one member, a domestic corporation. Such guidance may provide that the partnership can make the election if the partnership includes (in the manner prescribed by the Secretary) a disclosure of the name and taxpayer identification number of each of the disregarded entity and the corporation that is its sole member, and each of them is taken into account as if each were a statement recipient in determining whether the 100-or-fewer-statements criterion is met.

As another example, such guidance may provide that a partnership with a trust as a partner can make the election if the partnership includes (in the manner prescribed by the Secretary) a disclosure of the name and taxpayer identification number of the trustee, each person who is or is deemed to be an owner of the trust, and any other person that the Secretary determines to be necessary and appropriate, and each one of such persons is taken into account as if each were a statement recipient in determining whether the 100-or-fewer-statements criterion is met. Similar guidance may be provided with respect to a partnership with a partner that is a grantor trust, a former grantor trust that continues in existence for the two-year period following the death of the deemed owner, or a trust receiving property from a decedent's estate for a two-year period.

As a further example, to the extent that such rules are consistent with prompt and efficient collection of tax attributable to the income of partnerships and partners, such guidance may provide rules permitting election out in the case of a partnership (the first partnership) with one or more direct or indirect partners which are themselves partnerships. Under any such guidance with respect to tiered partnerships, the sum of all direct and indirect partners (including each partnership and its partners) may not exceed 100 persons with respect to which a section 6031(b) statement must be furnished, and each partner must be identified. That is, eligibility of the first partnership to make the election requires the first partnership to include (in the manner prescribed by the Secretary) a disclosure of the name and taxpayer identification number of each direct partner of the first partnership and each indirect partner (in-

[190] Sec. 6221(b)(1)(B).

cluding each partnership and its partners) in every tier, and requires that each is taken into account in determining whether the 100-or-fewer-statements criterion is met.

Requirement of consistency with partnership return

The centralized system imposes a consistency requirement. A partner on its return must treat each item of income, gain, loss, deduction or credit attributable to a partnership in a manner that is consistent with the treatment of such income, gain, loss, deduction, or credit on the partnership return.[191] An underpayment that results from a failure of a partner to conform to the partnership reporting of an item is treated as a math error on the partner's return and cannot be abated under section 6213(b)(2).[192] The underpayment may be subject to additions to tax.

Notice of inconsistent position

If the partnership has filed a return but the partner's treatment on the partner's return is (or may be) inconsistent with the partnership's return, or if the partnership has not filed a return, the math error treatment and nonabatement treatment do not apply if the partner files a statement identifying the inconsistent position.[193] Further, a partner is treated as having complied with the obligation to file a statement identifying the inconsistent position in the circumstance in which the partner demonstrates to the satisfaction of the Secretary that the treatment of the item on the partner's return is consistent with the treatment of the item on the statement furnished to the partner by the partnership, and the partner elects the application of this rule.

A final decision in an administrative or judicial proceeding with respect to a partnership under the centralized system is binding on the partnership and all partners of the partnership.[194] In contrast, a final determination in an administrative or judicial proceeding with respect to a partner's identified inconsistent position is not binding on the partnership if the partnership is not a party to the proceeding.[195] No inference is intended that the partnership is bound by any other proceeding to which it is not a party, such as an administrative or judicial proceeding with respect to a partner's unidentified inconsistent position.

Partners bound by actions of partnership; designation of partnership representative

For purposes of the centralized system, the partnership acts through its partnership representative. The partnership representative has the sole authority to act on behalf of the partnership under the centralized system.[196] Under the centralized system, the partnership and all partners of the partnership are bound by actions taken by the partnership.[197] Thus, for example, partners may not participate in or contest results of an examination of a partner-

[191] Sec. 6222(a).
[192] Sec. 6222(b).
[193] Sec. 6222(c).
[194] Sec. 6223(b).
[195] Sec. 6222(d).
[196] Sec. 6223(a).
[197] Sec. 6223(b).

ship by the Secretary. A partnership and all partners of the partnership are also bound by any final decision in a proceeding with respect to the partnership brought under the centralized system of subchapter C. Thus, for example, a settlement agreement entered into by the partnership, a notice of final partnership adjustment with respect to the partnership that is not contested, or the final decision of the court with respect to the partnership if the notice of final partnership adjustment is contested, bind the partnership and all partners of the partnership.

Each partnership is required to designate a partner (or other person) with a substantial presence in the United States as the partnership representative. A substantial presence in the United States enables the partnership representative to meet with the Secretary in the United States as is necessary or appropriate, and facilitates communication during the audit process and during any other proceedings in which the partnership is involved. In any case in which such a designation by the partnership is not in effect, the Secretary may select any person as the partnership representative.

Partnership Adjustments

Partnership adjustments by the Secretary

The centralized system provides that any adjustment to items of income, gain, loss, deduction, or credit of a partnership for a partnership taxable year, and any partner's distributive share thereof, are determined at the partnership level. Any tax attributable to these items is assessed and generally is collected at the partnership level as an imputed underpayment paid by the partnership.

Reviewed year and adjustment year

For purposes of the centralized system, the reviewed year means the partnership taxable year to which the item being adjusted relates. For example, in an examination by the Secretary of a partnership's taxable year 2018, 2018 is the reviewed year.[198]

The adjustment year means (1) in the case of an adjustment pursuant to the decision of a court (under the centralized system's judicial review provisions), the partnership taxable year in which the decision becomes final; (2) in the case of an administrative adjustment request, the partnership taxable year in which the administrative adjustment request is made; or (3) in any other case, the partnership taxable year in which the notice of final partnership adjustment is mailed.[199] For example, in the case of adjustments with respect to partnership taxable year 2018 resulting in an imputed underpayment assessed in 2020 that the partnership then litigates in Tax Court, the decision of which is not appealed and becomes final in 2021, the adjustment year is 2021.

Payment of imputed underpayment by the partnership

Any adjustment to items of income, gain, loss, deduction, or credit of a partnership for a partnership taxable year, and any partner's distributive share thereof, are determined at the partnership level. In the event of any adjustment by the Secretary in the

[198] Sec. 6225(d)(1).
[199] Sec. 6225(d)(2).

amount of any item of income, gain, loss, deduction, or credit of a partnership, or any partner's distributive share, that results in an imputed underpayment, the partnership is required to pay the imputed underpayment in the adjustment year.[200]

Interest at partnership level

Interest due is determined at the partnership level and accrues at the rate applicable to underpayments.[201]

Adjustment that does not result in imputed underpayment

Any adjustment by the Secretary in the amount of any item of income, gain, loss, deduction, or credit of a partnership, or any partner's distributive share, that does not result in an imputed underpayment is taken into account by the partnership in the adjustment year. The amount of the adjustment is treated as a reduction in non-separately stated income or an increase in non-separately stated loss (whichever is appropriate). It may also be appropriate to treat the amount of an adjustment as a reduction (or increase) in a separately stated amount of income, gain, loss, or deduction. The amount of an adjustment in a credit is taken into account as a separately stated item.[202]

Determination of imputed underpayment amount

An imputed underpayment of tax with respect to a partnership adjustment for any reviewed year is determined by netting all adjustments of items of income, gain, loss, or deduction and multiplying the net amount by the highest rate of Federal income tax applicable either to individuals or to corporations that is in effect for the reviewed year.[203] Any adjustments to items of credit are taken into account as an increase or decrease, as the case may be, in the figure resulting from this multiplication. Any net increase or decrease in loss is treated as a decrease or increase, respectively, in income. Netting is done taking into account applicable limitations, restrictions, and special rules under present law.

Examples

Example.—Assume that a partnership reports the following items on its return for taxable year 2018 (dollar amounts in thousands):

- rental income of $100
- depreciation deduction of <$70>
- interest expense deduction of <$20>
- deduction for compensation paid of <$50>

In an examination of the partnership's taxable year 2018, the Secretary determines that depreciation was <$80>, not <$70>, for the year. (Assume that this change does not affect depreciation in other taxable years.) The Secretary also finds that $5 of rental in-

[200] Sec. 6225(a)(1).
[201] Sec. 6621(a)(2). Rules relating to interest, penalties, and additions to tax are further described below.
[202] Sec. 6225(a)(2).
[203] Sec. 6225(b)(1). The rule for determining the imputed underpayment applies except as provided in subsection 6225(c), which provides that the Secretary shall establish procedures under which the imputed underpayment amount may be modified consistent with requirements imposed thereunder.

come was omitted, for total rental income of $105, not $100, for the year. The adjustment reflecting an increase of $5 of rental income is netted with the adjustment reflecting the <$10> change in the depreciation (both ordinary in character and not subject to differing limitations or restrictions). The resulting adjustment is a net increase in loss of <$5>. There is no imputed underpayment. For the adjustment year (not 2018, the reviewed year), the partnership has an increase in non-separately stated loss of <$5> (or a reduction in non-separately income of <$5>).

Example.—As another example, assume a partnership reports the following items on its return for taxable year 2019 (dollar amounts in thousands):

- ordinary income of $300
- long-term capital gain (from asset sales) of $125, long-term capital loss (from asset sales) of <$75>, for a net long-term capital gain of $50
- depreciation deduction of <$100>
- tax credit of $5

In an examination of the partnership's taxable year 2019, the Secretary adjusts these items as follows and finds:

- ordinary income of $500 (a $200 adjustment)
- long-term capital gain of $200 (a $75 adjustment) and long-term capital loss of <$25> (a <$50> adjustment), for a net long-term capital gain of $175 (a $125 adjustment)
- depreciation deduction of <$70> (a <$30> adjustment)
- tax credit of $3 (a <$2> credit adjustment)

These are netted under the provision as follows. The adjustments to ordinary income and to the ordinary depreciation deduction are netted: $200 minus <$30> yields $230. The adjustments to long-term capital gain and loss are netted: $75 minus <$50> yields $125. The adjustments total $355. Assume that the highest rate of Federal income tax applicable to individuals or corporations in 2019 is 39.6 percent. The product of $355 and 39.6 percent is $140.58. The credit adjustment of <$2> increases that figure, yielding an imputed underpayment of $142.58 (not taking into account possible modifications further described below). The partnership pays the imputed underpayment in the adjustment year.

Determining imputed underpayment amount: adjustments to distributive shares

In determining an imputed underpayment, any adjustment that reallocates the distributive share of any item from one partner to another is taken into account by disregarding any decrease in any item of income or gain and disregarding any increase in any item of deduction, loss, or credit.[204]

Example

For example, assume that a partnership has two partners, L and M. Under the partnership agreement, $100 of rental income is allocated to L and $70 of depreciation and interest deductions are allocated to M for the taxable year. The Secretary notifies the partnership and the partnership representative of an administrative pro-

[204] Sec. 6225(b)(2).

ceeding initiated at the partnership level with respect to the partnership's return for 2024. Assume that the Secretary determines that the $70 distributive share of depreciation and interest deductions should be reallocated from M to L. The imputed underpayment of the partnership is determined without decreasing the $100 of rental income by the $70 of depreciation and interest deductions. The adjustment is a $70 increase in income. Assume that the highest rate of Federal income tax applicable to individuals or corporations in 2024 is 39.6 percent. The product of $70 and 39.6 percent is $27.72, the amount of the imputed underpayment. However, the partnership may implement procedures for modifying the imputed underpayment as so determined.

Modification of imputed underpayment amount

When an audit of a partnership is commenced, the Secretary notifies the partnership and the partnership representative of the administrative proceeding initiated at the partnership level. The Secretary also notifies the partnership and the partnership representative of any proposed partnership adjustment developed during the proceeding.[205] The Secretary must establish procedures for modification of the amount of an imputed underpayment.[206] One or more modification procedures may be implemented by the partnership after the initiation of the administrative proceeding, including before any notice of proposed adjustment. These procedures include the filing of amended returns by reviewed year partners, determination of the imputed underpayment without regard to the portion of it allocable to a tax-exempt partner, and modification of the applicable highest tax rates, including determining the portion of an imputed underpayment to which a lower rate applies.[207] In addition, the Secretary may by regulations or guidance provide for additional procedures to modify imputed underpayment amounts on the basis of factors that the Secretary determines are necessary or appropriate to carry out the function of the modification provisions, that is, to determine the amount of tax due as closely as possible to the tax due if the partnership and partners had correctly reported and paid while at the same time to implement the most

[205] Sec. 6231(a)(1) and (2).
[206] Sec. 6225(c).
[207] See section 411 of the Protecting Americans from Tax Hikes Act of 2015 (Division Q of Pub. L. No. 114–113). Under the provision, certain section 469(k) passive activity losses can reduce the imputed underpayment of a publicly traded partnership under the centralized system. The imputed underpayment can be determined without regard to the portion of the underpayment that the partnership demonstrates is attributable to (*i.e.*, would be offset by) specified passive activity losses attributable to a specified partner. The amount of the specified passive activity loss is concomitantly decreased, and the partnership takes the net decrease into account as an adjustment in the adjustment year with respect to the specified partners to which the net decrease relates. A specified passive activity loss for any specified partner of a publicly traded partnership means the lesser of the section 469(k) passive activity loss of that partner which is separately determined with respect to the partnership (1) for the partner's taxable year in which or with which the reviewed year of the partnership ends, or (2) for the partner's taxable year in which or with which the adjustment year of the partnership ends. A specified partner is a person who continuously meets each of three requirements for the period starting with the partner's taxable year in which or with which the partnership reviewed year ends through the partner's taxable year in which or with which the partnership adjustment year ends. These three requirements are that the person is a partner of the publicly traded partnership; the person is an individual, estate, trust, closely held C corporation, or personal service corporation; and the person has a specified passive activity loss with respect to the publicly traded partnership.

efficient and prompt assessment and collection of tax attributable to the income of the partnership and partners.

Anything required to be submitted pursuant to the modification of the amount of an imputed underpayment must be submitted to the Secretary not later than the close of the 270-day period beginning on the date the notice of a proposed partnership adjustment is mailed, unless the 270-day period is extended with the consent of the Secretary.

Any modification of the amount of an imputed underpayment is made only upon approval of the modification by the Secretary.

Modification procedures: amended returns of reviewed year partners

Payments made by reviewed year partners with amended returns can reduce the amount of an imputed underpayment.[208] Procedures for modification provide that the amount of an imputed underpayment is determined without regard to the portion of the underpayment taken into account by payment of tax included with amended returns of the reviewed year partners. The amended return relates to the taxable year of the partner that includes the end of the reviewed year of the partnership. The amended return is to take into account all adjustments in the amount of any item of income, gain, loss, deduction, or credit of the partnership (or any partner's distributive share) properly allocable to each partner, along with changes for any other taxable year with respect to which any tax attribute is affected by reason of the adjustments. Payment of any tax due is to be included with the amended return. In the case of an adjustment that reallocates the distributive share of any item from one partner to another, this modification procedure is only available if amended returns for the reviewed year are filed by all partners affected by the adjustment.

Modification procedures: tax-exempt partners

Procedures for modification provide for determining the amount of the imputed underpayment without regard to the portion of it that the partnership demonstrates is allocable to a partner that would not owe tax by reason of its status as a tax-exempt entity for the reviewed year.[209] For this purpose, a tax-exempt entity means (1) the United States, any State or political subdivision thereof, any possession of the United States, or any agency or instrumentality of any of these, (2) an organization (other than a cooperative) that is exempt from Federal income tax, (3) any foreign person or entity, and (4) any Indian tribal government determined by the Secretary in consultation with the Secretary of the Interior to exercise governmental functions. Under this procedure for modification, the partnership demonstrates the amounts of adjustments that are allocable to the tax-exempt partner and the resulting portion of the imputed underpayment allocable to that partner.[210]

[208] Sec. 6225(c)(2).
[209] Sec. 6225(c)(3).
[210] Secs. 6225(c)(3) and 168(h)(2)(A).

Modification procedures: modification of applicable highest tax rates

Procedures for modification provide for taking into account a rate of tax lower than the highest rate of Federal income tax applicable either to individuals or to corporations that is in effect for the reviewed year, for certain types of taxpayers or types of income.[211]

The partnership may demonstrate that a portion of an imputed underpayment is allocable to a partner that is a C corporation, and for that C corporation partner, the highest marginal rate of Federal income tax (35 percent in 2016, for example) for ordinary income and capital gain[212] for the reviewed year is lower than the highest marginal rate of Federal income tax for individuals (39.6 percent in 2016, for example). For a C corporation, the highest marginal rate of Federal income tax is the highest rate of tax specified in section 11(b).

Similarly, the partnership may demonstrate that a portion of an imputed underpayment relates to an item of long-term capital gain or qualified dividend income that is allocable to a partner who is an individual, and that the highest rate of tax with respect to that item of long-term capital gain or qualified dividend income for the reviewed year (20 percent for 2016, for example) is lower than the highest rate of Federal income tax applicable to individuals for the reviewed year (39.6 percent in 2016, for example). The highest rate for the type of income and type of taxpayer applies under the modification. An S corporation is treated as an individual for this purpose.

In general, the portion of the imputed underpayment to which the lower rate applies with respect to a partner is determined by reference to the partner's distributive share of items of income, gain, loss, deduction, and credit to which the imputed underpayment relates. However, if the partner's distributive share differs among items, then the portion of the imputed underpayment to which the lower rate applies is determined by reference to the amount of the partner's distributive share of net gain or loss if the partnership had sold all of its assets at their fair market value as of the close of the reviewed year. For example, adjustments are made to a partnership's rental income from property A and its depreciation deductions with respect to property B. A corporate partner has a 20 percent distributive share of rental income from property A, a 15 percent distributive share of depreciation deductions from property B, and a 20 percent distributive share of any gain in the reviewed year. However, if the partnership had sold its assets at fair market value as of the close of the reviewed year, the gain would have been $100, and based on its capital account, the corporate partner's distributive share would have been $20. Thus, the portion of the imputed underpayment to which the lower rate applies with respect to the corporate partner is 20 percent.

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[211] Sec. 6225(c)(4).

[212] The Secretary has regulatory authority under the provision, including authority to acknowledge or identify the types of income, gain, deduction, and loss to which the lower rate applies. See also section 411 of the Protecting Americans from Tax Hikes Act of 2015 (Division Q of Pub. L. No. 114–113). A lower rate of tax may be taken into account in the case of either capital gain or ordinary income of a partner that is a C corporation.

Modification procedures: additional procedures

Additional procedures to modify the amount of an imputed underpayment may be provided by the Secretary on the basis of factors the Secretary determines are necessary or appropriate to carry out the purposes of the provision. These procedures allow partnerships to demonstrate tax attributes or information with respect to the reviewed year and with respect to reviewed year partners that could permit modification of the imputed underpayment to more closely approximate the amount of tax due with respect to the reviewed year if the partnership and partners had correctly reported and paid the tax due.

In the absence of regulations or guidance specifically addressing the manner in which these modifications or calculations are made, it is anticipated that partnerships will furnish to the Secretary the necessary documentation, data, and calculations to determine the amount of the reduction of the imputed underpayment with a reasonably high degree of accuracy.

Alternative to payment of imputed underpayment by partnership

As an alternative to partnership payment of the imputed underpayment in the adjustment year, the audited partnership may elect to furnish to the Secretary and to each partner of the partnership for the reviewed year a statement of the partner's share of any adjustments to income, gain, loss, deduction and credit as determined in the notice of final partnership adjustment.[213] In this case, each such partner takes these adjustments into account and pays the tax as provided under the provision.[214]

Payment by reviewed year partners in year that includes date of the statement

The reviewed year partner's tax is increased for the partner's taxable year that includes the date of the statement.

Amount of the reviewed year partner's adjustment

The reviewed year partner's tax is increased by an amount equal to the aggregate of the adjustment amounts as determined under the provision. This includes the amount by which the partner's tax would increase if the partner's distributive share of the adjustment amounts were included for the partner's taxable year that includes the end of the reviewed year, plus the amount by which the tax would increase by reason of adjustment to tax attributes in years after that year of the partner and before the year of the date of the statement. Tax attributes in any subsequent taxable year are required to be appropriately adjusted.

Penalties, additions to tax, additional amounts

Penalties, additions to tax, and additional amounts are determined at the partnership level;[215] each reviewed year partner is

[213] Sec. 6226(a).
[214] Sec. 6226(b).
[215] Secs. 6221 and 6226(c).

liable for its share of the penalty, addition to tax, and additional amount.[216]

Interest at partner level from reviewed year, with adjustments

In the case of an imputed underpayment for which the election under this provision is made, interest is determined at the partner level.[217] Interest is determined from the due date of the partner's return for the taxable year to which the increase is attributable. Interest is determined taking into account any increases attributable to a change in tax attributes for an intervening tax year. The rate of interest determined at the partner level is the underpayment rate as modified under the provision, that is, the rate is the sum of the Federal short-term rate (determined monthly) plus 5 percentage points.

Time and manner of making election

The partnership may make this election not later than 45 days after the notice of final partnership adjustment.[218] The election is revocable only with the consent of the Secretary. The election may be made whether or not the partnership files a petition for judicial review of the notice of final partnership adjustment.[219]

The partnership may make the election within 45 days from the notice of final partnership adjustment, and within 90 days from the notice of final partnership adjustment may file a petition for readjustment with the Tax Court, district court, or Court of Federal Claims.[220] Upon the final court decision, dismissal of the case, or settlement, the partnership is to implement the election by furnishing statements (at the time and manner prescribed by the Secretary) to the reviewed year partners showing each partner's share of the adjustments as finally determined. As part of any settlement, for example, it is contemplated that the Secretary may permit revocation of a previously made election, and the partnership may pay at the partnership level.

Time and manner of furnishing statement

The statement is to be furnished to the Secretary and to partners within such time and in such manner as is prescribed by the Secretary. In the absence of such guidance, the statements are to be furnished to the Secretary and to all partners within a reasonable period following the last day on which to make the election under this provision. The date the statement is furnished (as well as the date of the statement) is the date the statement is mailed, for this purpose.

Information furnished on statement to the Secretary and to partners

The statement furnished to the Secretary and to partners is to include the amounts of and tax attributes of the adjustments allocable to the recipient partner. Under regulatory authority, the Sec-

[216] Sec. 6226(c).
[217] Sec. 6226(c)(2).
[218] Sec. 6226(a)(1).
[219] Sec. 6226(d). See section 411 of the Protecting Americans from Tax Hikes Act of 2015 (Division Q of Pub. L. No. 114–113).
[220] Sec. 6234.

retary may require the statement to show the amount of the imputed underpayment allocable to the recipient partner. In addition, the statement is to include the name and taxpayer identification number of the recipient partner. The Secretary may require that the statement include such additional information as is necessary or appropriate to carry out the purposes of the provision, such as the address of the recipient partner and the date the statement is mailed.

Treatment of tiered partnerships and other tiered entities

Tiered partnerships.—In the case of tiered partnerships, a partnership that receives a statement from the audited partnership is treated similarly to an individual [221] who receives a statement from the audited partnership. That is, the recipient partnership takes into account the aggregate of the adjustment amounts determined for the partner's taxable year including the end of the reviewed year, plus the adjustments to tax attributes in the following taxable years of the recipient partnership. The recipient partnership pays the tax attributable to adjustments with respect to the reviewed year and the intervening years, calculated as if it were an individual (consistently with section 703), for the taxable year that includes the date of the statement. The recipient partnership, its partners in the taxable year that is the reviewed year of the audited partnership, and its partners in the year that includes the date of the statement, may have entered into indemnification agreements under the partnership agreement with respect to the risk of tax liability of reviewed year partners being borne economically by partners in the year that includes the date of the statement. Because the payment of tax by a partnership under the centralized system is nondeductible, payments under an indemnification or similar agreement with respect to the tax are nondeductible.

Deficiency dividends.—A recipient partner that is a RIC or REIT and that receives a statement from an audited partnership including adjustments for a prior (reviewed) year may wish to make a deficiency dividend [222] with respect to the reviewed year. Guidance coordinating the receipt of a statement from an audited partnership by a RIC or REIT with the deficiency dividend procedures is expected to be issued by the Secretary.

Administrative adjustment request by partnership

A partnership may file a request for an administrative adjustment in the amount of one or more items of income, gain, loss, deduction, or credit of the partnership for a partnership taxable year.[223] Following the filing of the administrative adjustment request, the partnership may apply most of the procedures for modification [224] in a manner similar to modification of an imputed underpayment under new section 6225(c). Like the partnership audit, tax resulting from the adjustment may be paid by the partners in

[221] See section 703, which states, "the taxable income of a partnership shall be computed in the same manner as in the case of an individual . . .".
[222] Sec. 860.
[223] Sec. 6227.
[224] Not including the modifications pursuant to filing of amended returns of reviewed year partners in new section 6225(c)(2).

the manner in which a partnership pays an imputed underpayment in the adjustment year under new section 6225. Alternatively, the adjustment may be taken into account by the partnership and partners, and the tax paid by reviewed year partners upon receipt of statements showing the adjustments, similar to new section 6226.[225] However, in the case of an adjustment (pursuant to a partnership's administrative adjustment request) that would not result in an imputed underpayment, any refund is not paid to the partnership; rather, procedures similar to the procedure for furnishing reviewed year partners with statements reflecting the requested adjustment apply, with appropriate adjustments.

Time for making administrative adjustment request

A partnership may not file an administrative adjustment request more than three years after the later of (1) the date on which the partnership return for the year in question is filed, or (2) the last day for filing the partnership return for that year (without extensions).

In no event may a partnership file an administrative adjustment request after a notice of an administrative proceeding with respect to the taxable year is mailed.

Tiered partnerships

In the case of tiered partnerships, a partnership's partners that are themselves partnerships may choose to file an administrative adjustment request with respect to their distributive shares of an adjustment. The partners and indirect partners that are themselves partnerships may choose to coordinate the filing of administrative adjustment requests as a group to the extent permitted by the Secretary.

Procedural Rules

In general[226]

The new centralized system provides rules governing notices, time limitations, restrictions on assessment and the imposition of interest and penalties in the context of a partnership adjustment.[227] The provisions include specific grants of regulatory authority to address the identification of foreign partners, the manner of notifying partners of an election out of centralized procedures, the manner in which a partnership representative is selected, and the extent to which the new centralized system may be applied before the generally applicable effective date.

Notice of proceedings and adjustments

The centralized system contemplates three types of principal notifications by the Secretary to the partnership and the partnership representative in the course of an administrative proceeding with respect to that partnership. The notifications also apply to any proceeding with respect to an administrative adjustment request filed

[225] Sec. 6227(b)(2); interest is computed at the underpayment rate (sec. 6621(a)(2)) without substituting "5 percentage points" for "3 percentage points" as under section 6226(c)(2)(C).
[226] Secs. 6231 through 6235.
[227] Secs. 6231–6235.

by a partnership.[228] These notices are (1) notice of any administrative proceeding initiated at the partnership level; (2) notice of a proposed partnership adjustment resulting from the proceeding; and (3) notice of any final partnership adjustment resulting from the proceeding. Such notices are sufficient if mailed to the last known address of the partnership representative or the partnership, even if the partnership has terminated its existence.

A notice of proposed adjustments informs the partnership of any adjustments tentatively determined by the Secretary and the amount of any imputed underpayment resulting from such adjustments. The issuance of a notice of proposed partnership adjustment begins the running of a period of 270 days in which to supply all information required by the Secretary in support of a request for modification. During that same period, the Secretary may not issue a notice of final partnership adjustment.[229] The Secretary is required to establish procedures and timeframes for the modification process in published guidance, which may include conditions under which extensions of time in which to submit final documentation of a modification request may be permitted by the Secretary.[230]

With the issuance of a notice of final partnership adjustment to the partnership, a 90-day period begins during which the partnership may seek judicial review of the partnership adjustment. The issuance of a notice of final partnership adjustment also marks the beginning of the 45-day period in which the partnership may elect the alternative payment procedures.[231] Further notices of adjustment or assessments of tax against the partnership with respect to the partnership taxable year that is the subject of the notice of final partnership adjustment are prohibited during the period in which judicial review may be sought or during which a judicial proceeding is pending (absent a showing of fraud, malfeasance, or misrepresentation of a material fact).[232]

Any notice of partnership adjustment may be rescinded by the Secretary, if the partnership consents. If the notice is rescinded, it is a nullity, and does not confer a right to seek judicial review, nor does it bar issuance of further notices.

Assessment, collection and payment

An imputed underpayment is assessed and collected in the same manner as if it were a tax imposed for the adjustment year under the Federal income tax.[233] The general provisions for assessment, collection and payment under subtitle F of the Code apply unless superseded by rules of the new centralized system. As a result, an imputed underpayment may be assessed against a partnership if the partnership agrees with the results of the examination, following the expiration of the 90th day after issuance of a notice of final partnership adjustment without initiation of judicial proceedings, or in the case of timely judicial proceedings, following the entry of final decision of such proceedings. If no court proceeding is initiated within the 90-day period, the amount that may be as-

[228] Secs. 6231(a) and 6227.
[229] Sec. 6231(a).
[230] Sec. 6225(c)(7).
[231] Sec. 6226.
[232] Sec. 6231(b).
[233] Sec. 6232.

sessed against the partnership is limited to the imputed underpayment shown in the notice.[234]

In the case of an administrative adjustment request for which the adjustment is determined and taken into account by the partnership in the partnership taxable year in which the request is made,[235] the imputed underpayment is required to be paid when the request is filed, and is assessed at that time. If the administrative adjustment request is subsequently audited and results in an imputed underpayment greater than that reported and paid with the originally filed request, the additional amount of the imputed underpayment may be assessed in the same manner and subject to same restrictions as any other imputed underpayment determined after examination.

Restrictions on assessment, levy, and collection

The centralized system provides a limitation on the time for assessment of a deficiency as well as levy and court proceedings for collection. Except as otherwise provided, no assessment of a deficiency may be made, and no levy or court proceeding for collection of any amount resulting from an adjustment may be made, begun, or prosecuted with respect to the partnership taxable year in issue before the close of the 90th day after the day that a notice of final partnership adjustment was mailed. If a petition for judicial review is filed,[236] no such assessment may be made and no such levy or court proceeding may be made, begun, or prosecuted before the decision of the court has become final.[237]

A premature action (i.e., one that violates the limitation on the time of assessment, levy, and court proceeding for collection) may be enjoined in the proper court, including the Tax Court.[238] This rule applies notwithstanding the general rule prohibiting suits for the purpose of restraining the assessment or collection of any tax.[239] The Tax Court has no jurisdiction to enjoin any such premature action unless a timely petition for judicial review has been filed,[240] and then only in respect of the adjustments that are the subject of the petition.

Several exceptions to the restrictions on assessment are provided.[241] First, rules similar to the math error authority under section 6213(b) are permitted as exceptions to the restrictions on assessment described above. The exceptions apply to instances in which a partnership is notified that adjustments to its return are necessary to correct errors arising from mathematical or clerical errors and in the case of a tiered partnership that fails to prepare its partnership return consistently with that of the partnership in which it is a partner. In the case of an inconsistent return position, the rules similar to those in section 6213(b) (providing for subsequent abatement of any resulting assessments if challenged within

[234] Sec. 6232(e).
[235] Secs. 6232(a) and 6227(b)(1).
[236] Sec. 6234.
[237] Sec. 6232(b).
[238] Sec. 6232(c).
[239] Sec. 7421(a).
[240] Sec. 6234.
[241] Sec. 6232(d).

60 days) are not applicable. Finally, a partnership may waive the restrictions on the making of any partnership adjustment.

Interest and penalties

Interest

In general, interest due is determined at the partnership level and accrues at the rate applicable to underpayments.[242] Two periods are relevant in computing the total interest due: the period in which the imputed underpayment of income tax exists, and the period attributable only to late payment of any imputed underpayment after notice and demand. For an imputed underpayment, interest accrues for the period from the due date of the return for the reviewed year until the due date of the adjustment year return, or, if earlier, payment of the imputed tax. If the imputed underpayment is not timely paid with the return for the adjustment year, interest is computed from the return due date for the adjustment year until payment.

If the partnership elects the alternative payment method under section 6226, under which the underpayment is determined at the partner level, the interest due is computed at the partner level. The underpayment interest begins to accrue from the due date of the return for the taxable year to which the increase is attributable, at a rate two percentage points higher than the rate otherwise applicable to underpayments.

Penalties

Generally, the partnership is liable for any penalty, addition to tax, or additional amount.[243] These amounts are determined at the partnership level as if the partnership were an individual who was subject to Federal income tax for the reviewed year, and the imputed underpayment were an actual underpayment or understatement for the reviewed year.

A penalty, addition to tax, or additional amount may apply with respect to an adjustment year return of a partnership in the event of late payment of an imputed underpayment, or, in the case of an election by the partnership under section 6226, with respect to the adjustment year return of a partner. In such cases, the penalty for failure to pay applies.[244] For purposes of accuracy-related and fraud penalties, the determination is made by treating the imputed underpayment as an underpayment of tax.[245]

Judicial review of partnership adjustment

A partnership may seek judicial review of a notice of final partnership adjustment within 90 days after the notice is mailed. Judicial review is available in the U.S. Tax Court, the Court of Federal Claims or a U.S. district court for the district in which the partnership has its principal place of business.

With respect to judicial review in either the Court of Federal Claims or a U.S. district court, jurisdiction is contingent on the

[242] Sec. 6621(a)(2).
[243] Sec. 6233(a)(1)(B).
[244] Secs. 6233(b)(3)(A) and 6651(a)(2).
[245] Secs. 6662, 6662A, 6663, and 6664.

partnership depositing with the Secretary, on or before the date of the petition, an amount equal to the full imputed underpayment. The deposit is not treated as a payment of tax other than for purposes of determining whether interest on any underpayment as ultimately determined would be due. The proceeding under this provision is a de novo proceeding, and determinations made pursuant to the proceeding are subject to review to the same extent as any other decision, decree or judgment of the court in question.

Once a proceeding is initiated, a decision to dismiss the proceeding (other than a dismissal because the notice of final partnership adjustment was rescinded under section 6231(c)), is a judgment on the merits upholding the final partnership adjustments.

Period of limitations on making adjustments

In general, the Secretary may adjust an item on a partnership return at any time within three years of the date a return is filed (or the return due date, if the return is not filed) or an administrative adjustment request is made. The time within which the adjustment is made by the Secretary may be later if a notice of proposed adjustment[246] is issued, because the issuance of a notice of proposed partnership adjustment begins the running of a period of 270 days in which the partnership may seek a modification of the imputed underpayment. Although the partnership generally is limited to 270 days from the issuance of that notice to seek a modification of the imputed underpayment, extensions may be permitted by the IRS. During the 270-day period, the Secretary may not issue a notice of final partnership adjustment.

After the timely issuance of a notice of proposed adjustment resulting in an imputed underpayment, the notice of final partnership adjustment may be issued no later than either the date which is 270 days after the partnership has completed its response seeking a revision of an imputed underpayment, or, if the partnership provides an incomplete or no response, no later than 330 days after the date of a notice of proposed adjustment.[247]

The partnership may consent to an extension of time within which a partnership adjustment may be made. In addition, the provision contemplates that the Secretary may agree to extend the period of time in which the request for modification is submitted, under procedures to be established for submitting and reviewing requests for modification. If an extension of the time within which to seek a modification is granted, a similar period is added to the time within which the Secretary may issue a notice of final partnership adjustment. The procedures for modifications of imputed underpayments are required to provide rules that exclude from any

[246] Sec. 6231.

[247] See section 411 of the Protecting Americans from Tax Hikes Act of 2015 (Division Q of Pub. L. No. 114–113), which rectifies the unintended conflict between section 6231 (barring the Secretary from issuing the notice of final partnership adjustment earlier than the expiration of the 270 days after the notice of a proposed adjustment) and section 6235 (requiring that a notice of final partnership adjustment be filed no later than 270 days after the notice of proposed adjustment in the case of a partnership that does not seek modification of the imputed underpayment). As amended, section 6235 provides that a notice of final partnership adjustment to a partnership that does not seek modification of an underpayment in response to a notice of proposed adjustment may be issued up to 330 days (plus any additional number of days that were agreed upon as an extension of time for taxpayer response) after the notice of proposed adjustment.

underpayment of tax the portion of adjustments that may have already been taken into consideration on amended returns filed by partners and for which the allocable underpayment of tax was paid.

Several exceptions similar to those generally applicable outside the context of partnerships are provided to the limitations period. In the case of a fraudulent return or failure to file a return, a partnership adjustment may be made at any time. If a partnership files a return on which it makes a substantial omission of income within the meaning of section 6501(e)(1)(A), the Secretary may make adjustments to the return within six years of the date the return was filed.

In addition, if a notice of final partnership adjustment described in section 6231 is mailed, the limitations period is suspended for the period during which judicial remedies under section 6234 may be pursued or are pursued and for one year thereafter. Where a partnership elects to apply section 6226, this provision operates to ensure that the period in which the Secretary may assess the resulting underpayment due from each partner is open for at least one year after proceedings at the partnership level have concluded. The partner who is responsible for paying an underpayment arising from the partnership reviewed year must compute such tax with respect to his taxable year in which or with which the partnership reviewed year ends, and pay the additional tax with the return for the year in which the partnership mails the statements to partners under section 6226. Because the additional tax arises from an adjustment at the partnership level that is binding on the partner, the partner may neither contest the merits of the partnership adjustment, nor may the partner claim the Secretary is time-barred with respect to such adjustment.

Examples

The interaction of the notice requirements of new section 6231 and the limitations period with regard to adjustments to partnership returns that result in imputed underpayments under new section 6235 is illustrated in this example regarding a partnership's taxable year 2018.

On March 15, 2019, it files a timely income tax return for the taxable year 2018. Absent any other activity by the Secretary or the partnership, the general three-year limitations period in which any item on the return may be adjusted expires in three years, on March 15, 2022.

On December 15, 2020, the Secretary notifies the partnership that it intends to initiate an administrative proceeding with respect to the 2018 partnership return. That notice neither shortens nor extends the period in which partnership adjustments may be made by the Secretary, but it ends the period in which the partnership may submit an administrative adjustment request with respect to that taxable year.

On September 15, 2021, the Secretary issues a notice of proposed adjustments that result in an imputed underpayment. Issuance of this notice triggers a period of 270 days during which the Secretary may not issue a notice of final partnership adjustment and within which the partnership must submit all required documentation in

support of a request for modification of the imputed underpayment. This 270-day periods ends on June 15, 2022, which is later than the expiration of the otherwise applicable limitations period. The deadline for issuance of a notice of final partnership adjustment will depend upon whether and how the partnership responds to the proposed notice of adjustments.

If nothing further is received from the partnership, the Secretary may issue a notice of final partnership adjustment no later than 330 days after the notice of proposed adjustments (i.e., within 60 days after the expiration of the 270-day period in which partnership was permitted to respond). Because the 330th day after September 15, 2021, falls on Sunday, August 14, 2022, the final date on which the Secretary may issue a notice of final partnership adjustment is Monday, August 15, 2022.[248]

The partnership may instead respond to the notice with a timely request for modification of the imputed underpayment but ask for additional time to complete its submission in support of the request for modification. For example, the Secretary may grant a timely request for 45 additional days, allowing the partnership until Monday, August 1, 2022, to submit its complete response.

- If the partnership fails to provide the required information by August 1, 2022 and no further extension is granted, then the Secretary may issue a notice of final partnership adjustment no later than September 30, which is 60 days after August 1, 2022 (the end of the 270-day period plus the additional time that was granted to the taxpayer to provide its complete response).
- If the partnership instead provides its complete response on August 1, a notice of final partnership adjustment may be issued up to 270 days after the date on which the information required by the Secretary was submitted, or April 28, 2023. During this 270-day period ending with April 28, 2023, the Secretary is expected to review the information that was submitted and revise the adjustments that were proposed if appropriate.

In the alternative, consider a variation of the above facts in which the partnership submits an administrative adjustment request on June 1, 2020 that corrects several errors on its timely-filed 2018 return. The administrative adjustment request results in an imputed underpayment of tax, which the partnership pays in full, with interest from March 15, 2019 (the filing date of the return) when it submits the administrative adjustment request. On December 15, 2020, the Secretary notifies the partnership that he will initiate an administrative proceeding with regard to taxable year 2018. On September 15, 2021, the Secretary issues a notice of proposed adjustments to the partnership 2018 return.

As a result of submitting an administrative adjustment request, the period in which partnership adjustments to the taxable year 2018 may be made is extended to June 1, 2023, the date that is three years from the date the administrative adjustment request is submitted. Because that date is later than all of the extensions described in the preceding scenarios, the Secretary may issue a notice

[248] See section 7503.

of final partnership adjustments on or before June 1, 2023, provided that such notice is issued after expiration of the 270-day period within which the partnership must respond to the notice of proposed adjustments issued September 15, 2021. The issuance of a notice of proposed adjustments cannot shorten the limitations period for making an adjustment to the partnership return.

Issues raised by the partnership in its administrative adjustment request may be the subject of inquiry by the Secretary in several ways. If the original partnership return may be the subject of an examination, the administrative adjustment request is likely to be reviewed as part of that process. Alternatively, the administrative adjustment request may be subject to examination on its own. Interest on an imputed underpayment accrues from March 15, 2019, the unextended due date of the 2018 timely return until payment, whether the examination was prompted by the return or solely by the administrative adjustment request. However, full payment of the reported underpayment reported on the administrative adjustment request, plus interest calculated through the date of the administrative adjustment requests, ends accrual of additional interest with respect to that portion of the underpayment ultimately determined that was reported on the administrative adjustment request. If an increase in the imputed underpayment reported by the partnership results from the relevant examination, the additional tax that should have been reported and paid with the administrative adjustment request submitted during 2020 will incur interest from March 15, 2019, unextended due date of the 2018 return, to the date the amount is paid.

In addition, the issues presented in the administrative adjustment request may be relevant to determining the correct treatment of items reported by the partnership on returns for other periods. For example, the year in which the request is filed may be subject to examination for issues related to the items that were the subject of the administrative adjustment request. In that case, information from taxable year 2018 is relevant, regardless of whether an examination of 2018 is opened. However, no imputed underpayment for 2018 may be determined without initiating an administrative proceeding with respect to that year.

Definitions and Special Rules

Definitions and special rules[249]

Partnership

The term partnership means any partnership required to file a return under section 6031(a). This includes any partnership described in section 761 that is required to file a return.

Partnership adjustment

The term partnership adjustment means any adjustment in the amount of any item of income, gain, loss, deduction, or credit of a partnership, or any partner's distributed share thereof.

[249] Sec. 6241.

Return due date

The term return due date means, with respect to the taxable year, the date prescribed for filing the partnership return for such taxable year (determined without regard to extensions).

Payments nondeductible

No deduction is allowed under the Federal income tax for any payment required to be made by a partnership under the centralized system of partnership audit, assessment, and collection.

Under the centralized system, the flowthrough nature of the partnership under subchapter K of the Code is unchanged, but the partnership is treated as a point of collection of underpayments that would otherwise be the responsibility of partners. The return filed by the partnership, though it is an information return, is treated as if it were a tax return where necessary to implement examination, assessment, and collection of the tax due and any penalties, additions to tax, and interest.

A basis adjustment (reduction) to a partner's basis in its partnership interest is made to reflect the nondeductible payment by the partnership of the tax. Specifically, present-law section 705(a)(2)(B) applies, providing that the adjusted basis of a partner's interest in a partnership is the basis of the interest determined under applicable rules relating to contributions and transfers, and decreased (but not below zero) by expenditures of the partnership that are not deductible in computing its taxable income and not properly chargeable to capital account. Concomitantly, the partnership's total adjusted basis in its assets is reduced by the cash payment of the tax. Thus, parallel basis reductions are made to outside and inside basis to reflect the partnership's payment of the tax. Partners, former partners, and the partnership may have entered into indemnification agreements under the partnership agreement with respect to the risk of tax liability of former or new partners being borne economically by new or former partners, respectively. Because the payment of tax by a partnership under the centralized system is nondeductible, payments under an indemnification or similar agreement with respect to or arising from the tax are nondeductible.

Partnerships having principal place of business outside the United States

For purposes of judicial review following a notice of final partnership adjustment, a principal place of business located outside the United States is treated as located in the District of Columbia.

Suspension of period of limitations on making adjustment, assessment or collection

The provision includes a rule similar to the present-law rule[250] to conform the automatic stay of the Bankruptcy Code (Title 11) with the limitations period applicable under the centralized system for partnership adjustments. Any statute of limitations period provided under the centralized system on making a partnership adjustment, or on assessment or collection of an imputed under-

[250] Sec. 6213(f).

payment, is suspended during the period the Secretary is prohibited by reason of the Title 11 case from making the adjustment, assessment, or collection. For adjustment or assessment, the relevant statute of limitations is extended for 60 days thereafter. For collection, the relevant statute of limitations is extended for six months thereafter.

In a case under Title 11, the 90-day period to petition for judicial review after the mailing of the notice of final partnership adjustment [251] is suspended during the period the partnership is prohibited by reason of the Title 11 case from filing such a petition for judicial review, and for 60 days thereafter.

Treatment where partnership ceases to exist

If a partnership ceases to exist before a partnership adjustment under the centralized system is made, the adjustment is taken into account by the former partners of the partnership, under regulations provided by the Secretary. Whether a partnership ceases to exist for this purpose is determined without regard to whether there is a technical termination of the partnership within the meaning of section 708(b)(1)(B). The successor partnership in a technical termination succeeds to the adjustment or imputed underpayment, absent regulations to the contrary. A partnership that terminates within the meaning of section 708(b)(1)(A) is treated as ceasing to exist. In addition, a partnership also may be treated as ceasing to exist in other circumstances or based on other factors, under regulations provided by the Secretary. For example, for the purpose of whether a partnership ceases to exist under new section 6241(7), a partnership that has no significant income, revenue, assets, or activities at the time the partnership adjustment takes effect may be treated as having ceased to exist.

Extension to entities filing partnership return

If a partnership return (Form 1065) is filed by an entity for a taxable year but it is determined that the entity is not a partnership (or that there is no entity) for the year, then, to the extent provided in regulations, the provisions of this subchapter are extended in respect of that year to the entity and its items of income, gain, loss, deduction, and credit, and to persons holding an interest in the entity.

For example, assume two taxpayers purport to create a partnership for taxable year 2018, and a Form 1065 is filed for that year. The partnership is the subject of an audit under the centralized system for 2018, and pursuant to the provisions for judicial review, the partnership is determined by a court not to exist as partnership. Nevertheless, the rules of the centralized system apply to the items of income, gain, loss, deduction and credit, and to the two taxpayers, in respect of 2018. An imputed underpayment may be collected from the purported partnership in the adjustment year pursuant to new section 6225. Alternatively, the purported partnership representative may elect (at the time and in the manner prescribed by the Secretary) under new section 6226 to issue statements to the two taxpayers, which purported to hold partnership

[251] Sec. 6234.

interests for the reviewed year. To the extent of the adjustments, each of the two taxpayer's tax may be increased for the taxpayer's taxable year that includes the date of the statement. In this situation, the amount of the increase for each of them is amount by which the taxpayer's tax would increase if the taxpayer's share of the adjustment amounts were included for the taxpayer's taxable year that includes the end of the reviewed year, plus the amount by which the tax would increase by reason of adjustment to tax attributes in years after that year of the taxpayer and before the year of the date of the statement.

Related provisions

Binding nature of partnership adjustment proceedings

The provision clarifies that the merits of an issue that is the subject of a final determination in a proceeding brought under the centralized system[252] is among the issues that are precluded from being raised at a collection due process hearing (in connection with the right to, and opportunity for, such a hearing prior to a levy on any property or right to any property under present law).[253] The provision does not restrict the authority of the Secretary to permit an opportunity for administrative review, similar to the Collection Appeals Program,[254] nor does it limit a partner's right to seek review of the conduct of collection measures, such as whether notices of Federal tax lien or notice of intent to levy were timely issued.

For example, assume that a partnership is audited with respect to taxable year 2018. One of the adjustments reflects the partnership's omission of income of $1,000 in calculating partnership taxable income. Following receipt of the notice of final partnership adjustment, the partnership decides not to litigate. The partnership elects to issue statements to reviewed year partners, whose tax is increased for the partner's taxable year that includes the date of the statement, 2021. Reviewed year partner A's adjustment is $100, resulting in an increase in tax of $35, but partner A does not pay the increased amount of tax. The time for the partnership to litigate the adjustments has elapsed and the notice of final partnership adjustment is a final determination. Prior to any levy on any property or right to any property of partner A in connection with collection of the $35 tax, partner A has the right to and is afforded the opportunity for a hearing (the collection due process hearing). At the hearing, partner A may not raise the issue of whether the $1,000 (or A's $100 share of it) was properly includable in determining partnership taxable income, because a final determination

[252] That is, a proceeding brought under subchapter C of chapter 63 of the Code.

[253] Section 6330 establishes the requirement that the IRS provide notice of potential collection action and offer an opportunity for a hearing before an impartial officer, and identifies which issues may be raised at such hearing and which are precluded. Issues permitted to be raised include the underlying liability only if the taxpayer did not receive a notice of deficiency or otherwise have an opportunity to contest the liability. Prior to amendment, the issues that were precluded listed those that were the subject of any previous administrative or judicial proceeding. Treas. Reg. 301–6330. The Secretary's power to levy is set forth in present-law section 6331.

[254] For example, under TEFRA, the IRS permits partners to raise computational issues, interest abatement questions and other collection due process rights in administrative appeals in order to assure consistency in the handling of the cases, even though the partners are precluded from questioning the substance of the partnership adjustment. See Internal Revenue Manual, paragraph 8.22.8.19, TEFRA Partnerships.

with respect to the issue was made in a proceeding brought under the centralized system. The result is the same if the partnership had decided to seek judicial review and the final determination of the court is that the $1,000 is includable in determining partnership taxable income.

Restriction on authority to amend partner information statements

The provision provides that partner information returns (currently Schedules K–1) required to be furnished by the partnership[255] may not be amended after the due date of the partnership return to which the partner information returns relate. The due date takes into account the permitted extension period. For example, the Schedules K–1 furnished by a partnership with respect to its taxable year 2020 may not be amended after the due date for the partnership 2020 return. If the partnership has a calendar taxable year, the due date for its partnership 2020 return is September 15, 2021 (taking into account the permitted 6-month extension following the due date of March 15, 2021), after which date the Schedules K–1 for 2020 may no longer be amended.[256] The partnership may, however, file an administrative adjustment request pursuant to new section 6227, and the partnership may pay any resulting imputed underpayment at the partnership level.

Example

For example, assume that a partnership files its Form 1065 for taxable year 2020 on March 15, 2021. On November 3, 2021, the partnership discovers an omission from income for 2020. The partnership may not issue amended Schedules K–1 to its partners for 2020. However, the partnership may file an administrative adjustment request and pay the underpayment consistently with new section 6227(b)(1) for the partnership taxable year in which the administrative adjustment request is made. In this situation, the partnership does not furnish amended Schedules K–1 to the partners and the partners do not file amended Federal and State income tax returns with respect to the omitted income.[257]

Effective Date

The provision applies to returns filed for partnership taxable years beginning after December 31, 2017. The provision relating to administrative adjustment requests applies to requests with respect to returns filed for partnership taxable years beginning after December 31, 2017. The provision relating to the election of a partnership to furnish statements to partners (section 6226) applies to

[255] The requirement of furnishing partner information returns is imposed by section 6031(b). See section 411 of the Protecting Americans from Tax Hikes Act of 2015 (Division Q of Pub. L. No. 114–113), correcting a conforming amendment to strike the last sentence of section 6031(b) under prior law, which sentence related to repealed provisions on electing large partnerships.

[256] This rule does not, however, preclude the filing of amended returns of reviewed-year partners pursuant to the procedure for modification of an imputed underpayment in section 6225(c)(2).

[257] The partnership that files the administrative adjustment request is not precluded from furnishing under section 6227(b)(2) an adjusted statement (similar to a Schedule K–1) to each reviewed-year partner, who is then required to pay tax attributable to the partnership adjustment (as provided under guidance provided by the Secretary).

elections with respect to returns filed for partnership taxable years beginning after December 31, 2017.

A partnership may elect for the provisions of the centralized system (other than the election out under section 6221(b)) to apply to any return of the partnership filed for partnership taxable years beginning after the date of enactment and before January 1, 2018. This election is made at such time and in such form and manner as the Secretary of the Treasury may prescribe. A partnership may not elect out of the centralized system under section 6221(b) in combination with this election.

A partnership may choose to make this election, for example, to be eligible before 2018 to pay at the partnership level, to obviate the need to furnish amended Schedules K–1 to correct a partnership-level error, or to obviate the need for partners receiving amended Schedules K–1 to file amended Federal and State income tax returns. A partnership may not elect out of the centralized system under section 6221(b) in combination with this election.

B. Partnership Interests Created by Gift (sec. 1102 of the Act and secs. 704(e) and 761(b) of the Code)

Present Law

Under present law, a partnership includes an unincorporated organization that carries on any business, financial operation, or venture which is not otherwise treated as a trust, estate, or corporation under the Internal Revenue Code.[258] The Supreme Court has stated that the test of a partnership is "whether considering all the facts . . . the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise".[259] A partner means a member of a partnership.[260]

Present law also provides that the manner in which a person acquires a capital interest is not determinative of whether that person is recognized as a partner for income tax purposes. If he owns a capital interest in a partnership in which capital is a material income-producing factor, whether or not the interest was derived by purchase or gift from any person, the owner is treated as a partner.[261] The predecessor of this provision was enacted in 1951 to prevent the IRS from denying partner status to a taxpayer who shared actual ownership of the partnership's income-producing capital on the basis that the interest was acquired from a family member.[262] According to the legislative history, "Your committee's amendment makes it clear that, however the owner of a partnership interest may have acquired such interest, the income is taxed to the owner, if he is the real owner. If the ownership is real, it does not matter what motivated the transfer to him or whether the business benefitted from the entrance of the new partner."[263] The focus of the legislation was on which party (transferor or transferee) actually owns a partnership interest, not on whether a par-

[258] Sec. 761(a). See also sec. 7701(a)(2).
[259] *Commissioner v. Culbertson*, 337 U.S. 733, 742 (1949).
[260] Sec. 761(b).
[261] Sec. 704(e)(1).
[262] Pub. L. No. 82–183, sec. 340(a).
[263] S. Rep. No. 781, 82d Cong., 1st Sess., 38, 39 (1951): H.R. Rep. No. 586, 82d Cong., 1st Sess. 32 (1951).