TECHNICAL EXPLANATION OF THE TAX TECHNICAL CORRECTIONS ACT OF 2016

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of the
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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a technical explanation of the tax technical corrections including those with respect to partnership audits, other corrections, and clerical and deadwood corrections contained in the Tax Technical Corrections Act of 2016, as introduced on December 6, 2016, in the House of Representatives as H.R. 6439 and in the Senate as S. 3506.

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[1] This document may be cited as follows: Joint Committee on Taxation, *Technical Explanation of the Tax Technical Corrections Act of 2016* (JCX-91-16), December 6, 2016. This document can be found on the Joint Committee on Taxation website at www.jct.gov.

DESCRIPTION OF THE TAX TECHNICAL CORRECTIONS ACT OF 2016

The bill includes technical corrections, other corrections, and clerical and deadwood corrections to recently enacted tax legislation. Except as otherwise provided, the amendments made by the technical corrections and other corrections contained in the bill take effect as if included in the original legislation to which each amendment relates.

A. Title I − Tax Technical Corrections

Amendments relating to the Protecting Americans from Tax Hikes ("PATH") Act of 2015 (Division Q of the Consolidated Appropriations Act, 2016)

Transit parity (Act sec. 105).−Under Code section 132(f)(2) as in effect before the changes made by the Act, the monthly limit on the fringe benefit exclusion for employer-provided parking was $175, and the monthly limit on employer-provided benefits for mass transit and van pooling combined was $100. These monthly limits were indexed under Code section 132(f)(6) using a base year determined by when the particular monthly limit became effective – a base year of 1998 for parking and 2001 for transit/vanpooling. Parity between the exclusions was provided on a temporary basis from 2009 through 2014. The Act created permanent parity in the exclusions by changing the monthly transit/vanpooling limit in Code section 132(f)(2) to $175. However, the Act failed to include a conforming change to repeal the base year rule in Code section 132(f)(6) for transit/vanpooling. The provision repeals the transit/vanpooling base year rule.

Research credit: not reinstate alternative incremental credit (Act sec. 121).−The alternative incremental credit expired in 2008. The provision clarifies that the alternative incremental credit is not reinstated by the Act, and makes conforming changes.

Bonus depreciation (Act sec. 143).−The provision clarifies that, among the criteria in the Act defining certain property having a longer production period that is treated as qualified property, the requirement that the property be acquired pursuant to a written contract before 2020 requires that the contract be a written binding contract. This corrects an unintended error which changed prior law.

The provision clarifies that the preproductive period under Code section 168(k)(5)(B)(ii) is consistent with the preproduction period under Code section 263A(e)(3).

The provision clarifies that, under the Act's phase-down with respect to the special rules for certain plants bearing fruits and nuts, the phase-down percentages apply to specified plants that are planted or grafted in 2018 (40 percent) and 2019 (30 percent), not grafted to a plant that has already been planted before 2018 or 2019, respectively.

The Act extends and modifies the additional first-year depreciation deduction for five years, generally through 2019 (through 2020 for certain longer-lived and transportation property ("LLTP")). The 50-percent allowance is phased down for property placed in service in taxable years beginning after 2017 (after 2018 for LLTP). The provision clarifies that for LLTP placed in service in 2018, 50 percent applies to the entire adjusted basis, and that for LLTP placed in service in 2019, 40 percent applies to the entire adjusted basis.

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The provision clarifies that if, for a taxable year, a taxpayer makes both an election under Code section 168(k)(7) not to claim bonus depreciation for all property in a particular class of property and an election under Code section 168(k)(4) to claim AMT credits in lieu of bonus depreciation, Code section 168(k)(4) does not apply to property in the particular class. This corrects an unintended error which changed prior law.

Election out of accelerated recovery periods for qualified Indian reservation property (Act sec. 167).−As amended by the Act, Code section 168(j) permits taxpayers to elect out of the otherwise applicable accelerated recovery periods in the case of qualified Indian reservation property. In general, if section 168(j) applies, there is no AMT adjustment (see section 168(j)(3)). The provision clarifies that no AMT adjustment applies in the case of qualified Indian reservation property if the taxpayer makes the election out.

Failure to furnish correct payee statements (Act sec. 202).−The provision clarifies Code section 6722(c)(3)(A), relating to failure to furnish correct payee statements, to refer to payee statements (rather than information returns) that are furnished (rather than filed). A corresponding change in the effective date stated in the Act refers to statements that are furnished (rather than provided).

Requirements for the issuance of Individual Taxpayer Identification Numbers ("ITINs") (Act sec. 203).−The provision clarifies that community-based Certifying Acceptance Agents are among the entities that are available to individuals living abroad who wish to obtain ITINs for purposes of meeting their U.S. tax filing obligations.

The provision clarifies that the expiration of ITINs that have not been used for three consecutive taxable years is to occur on the date following the due date of the tax return for such third consecutive taxable year. For ITINs issued prior to January 1, 2013, the ITIN will expire on the applicable date, or if earlier, the day following the due date of the tax return for the third consecutive taxable year such ITIN was not used on a return. In the event that such an ITIN has not been used for three (or more) consecutive taxable years on the tax return due date for the 2015 taxable year, such ITIN shall expire on the day following that date.

The provision clarifies that the effective date of section 203 of the Act, which provides that Act section 203 is effective for ITIN applications made after the date of enactment, does not prevent the provision relating to outstanding ITINs from taking effect.

Retroactive claims of credits (Act secs. 204, 205, and 206).−The provision conforms a reference in Code section 24(e)(2) to the taxpayer identification number (not to the identifying number). The provisions remove special effective date rules in each of these Act sections that have no practical effect.

Effective date for treatment of credits for certain penalties (Act sec. 209).−The Act inadvertently failed to state the effective date for the rule providing a reasonable cause exception for erroneous claims for refund or credit. The provision states that the effective date is for claims filed after the date of enactment of the Act.

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Making American Opportunity Tax Credit permanent (Act secs. 102, 206, 207, 208, and 211).−The provision reflects the permanent extension of the American Opportunity Tax Credit by eliminating deadwood and consolidating the provisions of Code section 25A.

Restriction on tax-free distributions involving Real Estate Investment Trusts ("REITs") (Act sec. 311).−The provision clarifies that, for purposes of Code section 355(h)(2)(B), control of a partnership means ownership of at least 80 percent of the profits interests and at least 80 percent of the capital interests. That is, control is not limited to exactly 80 percent ownership.

Ancillary personal property of a REIT (Act sec. 318).−As amended by the Act, Code section 856(c)(9) treats ancillary personal property as a real estate asset for purposes of the REIT 75 percent asset test to the extent that rents attributable to such ancillary personal property are treated, under a separate provision, as rents from real property. The provision makes two conforming changes with respect to the REIT income tests. First, the provision treats gain from the sale or disposition of such ancillary personal property as gain from the sale or disposition of a real estate asset for purposes of the REIT income tests. Second, the provision treats gain from the sale or disposition of certain obligations secured by mortgages on both real property and personal property as gain from the sale or disposition of real property for purposes of the REIT income tests.

Exception from Foreign Investment in U.S. Real Property Tax Act ("FIRPTA") for certain stock of REITs (Act sec. 322).−The provision restates provisions of Code section 897(k) as amended, makes clerical conforming changes, and strikes a modification to a repealed provision.

Further, under Code section 897(k) as amended, the provision addresses the definition of a qualified collective investment vehicle that is eligible for benefits of a comprehensive income tax treaty with the United States that includes an exchange of information program. Specifically, the provision clarifies that the definition can be met only if the dividends article in the treaty imposes conditions on the benefits allowable in the case of dividends paid by a REIT.

The provision clarifies the effective date for the determination of domestic control by stating that the rule applies with respect to each testing period ending on or after the date of enactment (not that the rule takes effect on the date of enactment).

FIRPTA exception for qualified foreign pension funds (Act sec. 323).−As amended by the Act, Code section 897(l)(1) provides that Code section 897 does not apply (i) to any United States real property interest held directly (or indirectly through one or more partnerships) by, or (ii) to any distribution received from a REIT by, a qualified foreign pension fund or an entity all the interests of which are held by a qualified foreign pension fund. The provision clarifies that, for purposes of Code section 897, a qualified foreign pension fund is not treated as a nonresident alien individual or as a foreign corporation; in other words, in determining the U.S. income tax of a qualified foreign pension fund, Code section 897 does not apply. The provision provides that, also for that purpose, an entity all the interests of which are held by a qualified foreign pension fund is treated as such a fund.

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As amended by the Act, Code section 897(l)(2) establishes a five-prong definition of the term “qualified foreign pension fund.” The provision revises the second prong of the definition to clarify that a government-established fund to provide public retirement or pension benefits may qualify, as well as a fund established by more than one employer to provide retirement or pension benefits to their employees, such as a multiple-employer or multiemployer plan. In addition, the provision makes clarifying changes to the fourth and fifth prongs of the definition.

Election of certain small insurance companies to be taxed only on taxable investment income (Act sec. 333).–As amended by the Act, Code section 831(b) requires that an otherwise eligible electing insurance company meet one of two diversification requirements. The first requires that no more than 20 percent of the company’s net (or if greater, direct) written premiums for the taxable year is attributable to any one policyholder. The second, applicable if the first is not met, requires that no person holds (directly or indirectly) aggregate interests in the company that constitute a percentage of the entire interest in the company that is more than a de minimis percentage higher than the percentage of interests in specified assets with respect to the company held (directly or indirectly) by a specified holder.

The provision clarifies the first diversification rule to provide a look-through rule with respect to an intermediary (for example, an aggregate fund). Specifically, the provision provides that in the case of reinsurance or any fronting, intermediary, or similar arrangement, a policyholder means each policyholder of the underlying direct written insurance with respect to the reinsurance or arrangement.

The provision clarifies the determination of percentages under the second diversification rule by making the determination with respect to relevant specified assets. They are defined (with respect to any specified holder with respect to any insurance company) to mean the aggregate amount of the specified assets, with respect to the insurance company, any interest in which is held directly or indirectly by a spouse or specified relation. The provision further clarifies that relevant specified assets do not include any specified asset that was acquired by the spouse or specified relation by bequest, devise, or inheritance from a decedent for a two-year period. Treasury Department guidance under the provision may provide that factors such as ownership, premiums, gross revenue, and factors taken into account under applicable State law for assessing risk are taken into account, to the extent this is consistent with the purpose of the provision to accurately determine percentages based on the real economic arrangement among the parties.

Amendments relating to Division P of the Consolidated Appropriations Act, 2016

Treatment of transportation costs of independent refiners (Act sec. 305).−The provision clarifies that Code section 199(c)(3)(C) applies for purposes of calculating qualified production activities income under Code section 199(c) and for purposes of calculating oil related qualified production activities income under Code section 199(d)(9).

The provision clarifies that an independent refiner may elect to apply section 199(c)(3)(C) to its oil transportation costs for purposes of calculating its deduction under Code section 199 (i.e., it is not required to apply the provision to its oil transportation costs). It is

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anticipated that the Secretary will issue guidance prescribing the manner in which such election shall be made.

Amendments relating to the Fixing America's Surface Transportation Act (2015)

Revocation or denial of passport in case of certain unpaid taxes (Act sec. 32101).−The Act provides for judicial review of the Secretary's certification that an individual has a seriously delinquent tax debt, either in a U.S. district court or in the Tax Court. The provision clarifies that the party against whom a Tax Court petition is filed is the Commissioner of the Internal Revenue Service. The provision also provides a tie-breaker rule clarifying that the court first acquiring jurisdiction over the action has sole jurisdiction, and corrects a cross reference.

Amendments relating to the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015

Consistent value for transfer and income tax purposes (Act sec. 2004).−The Act generally requires that an heir who inherits property from a decedent claim a basis no greater than the final value of the property for estate tax purposes (new Code section 1014(f)). New Code section 6662(b)(8) imposes a penalty in the case of an inconsistent estate basis. There is an inconsistent estate basis if the basis of property claimed on a return exceeds the basis as determined under the consistency requirement set forth in new Code section 1014(f). The penalty could be viewed as applying when an heir claims a basis higher than the final estate tax value by reason of making basis adjustments relating to post-acquisition events (e.g., improvements to the property). This result is not intended. The provision modifies the definition of inconsistent estate basis to avoid this unintended result.

Mass Transit Account ("MTA") financing (Act sec. 2008).−The Act changes the taxation of liquefied natural gas (LNG) and liquefied petroleum gas (LPG) from a per-gallon basis to an energy-equivalent basis. That is, the Act provides that the tax is based on the LNG energy equivalent to a gallon of diesel (DGE) (24.3 cents per DGE, which is 6.06 pounds of LNG), and on the LPG energy equivalent to a gallon of gasoline (GGE) (18.3 cents per GGE, which is 5.75 pounds of LPG). Code section 9503(e)(2) allocates 1.86 cents per gallon of LNG and 2.13 cents per gallon of LPG to the MTA of the Highway Trust Fund, but the Act does not specifically conform the per-gallon basis to an energy-equivalent basis for purposes of the allocation. The provision conforms the per-gallon basis in Code section 9503(e)(2) to the energy-equivalent basis, using DGE for LNG and GGE for LPG, to reflect the energy-equivalent basis used for the taxes imposed on LNG and LPG.

Amendments relating to the Stephen Beck, Jr., ABLE Act of 2014

Inflation adjustment for certain civil penalties under the Internal Revenue Code of 1986 (Act sec. 208).−The Act provides an annual inflation adjustment for fixed-dollar civil tax penalties in the case of: (i) Code section 6651(a), failure to file a tax return; (ii) Code section 6652(c), failure to file or disclose information returns by exempt organizations and certain trusts, (iii) Code section 6695, preparation of tax returns for other persons, (iv) Code section 6698, failure to file a partnership return, (v) Code section 6699, failure to file an S corporation return,

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(vi) Code section 6721, failure to file correct information returns, and (vii) Code section 6722, failure to furnish correct payee statements. The provision clarifies that the effective date of the annual inflation adjustments added to these civil penalties generally is for returns required to be filed, and statements required to be furnished, after December 31, 2014, and in the case of the annual inflation adjustment for penalties relating to preparation of tax returns for other persons, is for returns or claims for refund filed after December 31, 2014.

Amendments relating to the American Taxpayer Relief Act of 2012

Reference in definition of a deficiency to American Opportunity Tax Credit (Act sec. 104).−The provision conforms a reference in Code section 6211(b)(4)(A), relating to the definition of a deficiency, to a provision of the American Opportunity Tax Credit that was renumbered by the Act.

Amendments relating to the United States–Korea Free Trade Agreement Implementation Act (2011)

Increase in penalty on paid preparers who fail to comply with earned income tax credit due diligence requirements (Act sec. 501).−The provision clarifies that the effective date of the Code section 6695(g) penalty increase is for documents prepared (not returns required to be filed) after December 31, 2011.

Amendment relating to SAFETEA-LU

Penalty relating to signs (Act sec. 1125).–Persons engaged in distilled spirits operations are required to place and keep conspicuously on the outside of such place of business a sign showing the name of such person and denoting the business, or businesses, in which engaged. Code section 5681 imposes penalties for failure to post a required sign and posting or displaying a false sign. Under Code section 5681(b), a wholesale dealer in liquors may display a distilled spirits operations sign only if that person has paid the special occupational tax applicable to those wholesalers, payment of the tax being the indication that such person was eligible to post such a sign. SAFETEA-LU repealed the special occupational taxes, but did not make a conforming change to the penalty provision under 5681(b). The provision corrects the outdated reference in the penalty for displaying a false sign. Specifically, the provision modifies Code section 5681(b) to provide that a wholesale dealer in liquors may post a sign indicating that it is engaged in distilled spirits operations only if that person has complied with the recordkeeping requirements required by Code section 5121(a) and the registration requirements under Code section 5124.

Amendment relating to the American Jobs Creation Act of 2004

Rural electric cooperatives (Act sec. 319).–Code section 501(c)(12) of the Code provides an income tax exemption for rural electric cooperatives if at least 85 percent of the cooperative's income consists of amounts collected from members for the sole purpose of meeting losses and expenses of providing service to its members. The Energy Policy Act of 2005 made permanent a rule to exclude from the 85 percent test income from transactions related to open access transmission if approved by the Federal Energy Regulatory Commission ("FERC"). FERC regulates transmission lines in all States except Alaska, Hawaii and most of Texas. Because of an oversight, only transmission systems in Texas received the treatment

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accorded to FERC-regulated electric cooperatives. Electric cooperatives in Alaska are regulated by the Regulatory Commission of Alaska ("RCA"). Regulated utilities in Alaska with an RCA approved open access transmission tariff modeled after FERC should have received the same tax treatment as their similarly situated counterparts in the other States. The provision clarifies that that such utilities in Alaska and Hawaii are treated the same as those in Texas for purposes of the exclusion from the 85 percent test.

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B. Title II − Technical Corrections Related to Partnership Audit Rules (sec. 1101 of the Bipartisan Budget Act of 2015 and secs. 6221-6241 of the Code)

The provisions correct and clarify provisions relating to the partnership audit rules enacted in the Bipartisan Budget Act of 2015, as amended by the PATH Act of 2015, to express the intended rule. Section and chapter references are to the Internal Revenue Code of 1986 unless otherwise indicated.

Scope of adjustments subject to partnership audit rules (sec. 201 of the bill and secs. 6241(2) and (9) and 6221 of the Code)

The provision clarifies the scope of the partnership audit rules. The provision eliminates references to adjustments to partnership income, gain, loss, deduction, or credit, and instead refers to partnership-related items, defined as any item or amount with respect to the partnership that is relevant in determining the income tax liability of any person, without regard to whether the item or amount appears on the partnership's return and including an item or amount relating to any transaction with, basis in, or liability of, the partnership. Thus, these partnership audit rules are not narrower than the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") partnership audit rules, but rather, are intended to have a scope sufficient to address those items described as partnership items, affected items, and computational items in the TEFRA context in Treasury Regulations sections 301.6231(a)(3), 301.6231(a)(5), and 301.6231(a)(6), as well as any other items meeting the statutory definition of a partnership-related item.

For example, because a partnership-related item includes an item or amount relating to any transaction with the partnership, an item or amount relating to a partner's transaction with a partnership other than in his capacity as a member of the partnership (which is considered as occurring between the partnership and one who is not a partner under section 707) is a partnership-related item. As another example, because a partnership-related item includes an item or amount relating to basis in the partnership, an item or amount relating to the determination of the adjusted basis of a partner's interest in the partnership or relating to the basis of the partnership in partnership property is a partnership-related item. As a further example, because a partnership-related item includes an item or amount relating to liability of the partnership, an item or amount relating to the determination of partnership liabilities or to the effect on a partner of a decrease or increase in a partner's share of partnership liabilities is a partnership-related item.

The provision clarifies that the partnership audit rules do not apply to taxes imposed, or to amounts required to be deducted or withheld, under Code chapters 2 (tax on self-employment income), 2A (tax on net investment income), 3 (withholding tax on nonresident alien individuals or foreign corporations) or 4 (withholding tax for certain foreign accounts). However, any partnership adjustment determined under the income tax is taken into account for purposes of determining tax under these chapters of the Code to the extent that the partnership adjustment is relevant to the determination.

For example, if a partnership adjustment results in a change in the amount of income of an individual from a partnership, the change is reflected as required under the rules of chapter 2 in the calculation of the individual's net earnings from self-employment with respect to the

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partnership, and the chapter 2 tax may be collected through a process that is outside the partnership audit rules.

In determining the amount of any deficiency, adjustments to partnership-related items are made only as provided under the partnership audit rules (Subchapter C of Chapter 63 of the Code). Conforming references to partnership-related items are made in provisions of the partnership audit rules.

Netting in the determination of imputed underpayments (sec. 202 of the bill and sec. 6225(a) and (b) of the Code)

When the Secretary makes adjustments to any partnership-related item with respect to the reviewed year of a partnership, if the adjustments result in an imputed underpayment, the partnership pays an amount equal to the imputed underpayment, and if the adjustments do not result in an imputed underpayment, the adjustments are taken into account by the partnership in the adjustment year and passed through to the adjustment year partners. The provision clarifies this rule by conforming the language referring to partnership-related items and by striking erroneous references to separately stated income or loss.

The provision clarifies the manner of netting items to determine the amount of an imputed underpayment of a partnership. The provision clarifies that items of different character (capital or ordinary), for example, are not netted together in determining the amount of an imputed underpayment. Rather, an imputed underpayment of a partnership with respect to a reviewed year is determined by the Secretary by appropriately netting all partnership adjustments for that year and by applying the highest rate of tax in effect for the reviewed year under section 1 or 11.

In the case of partners' distributive shares, like items within categories under section 702(a)(1)-(8) are separately netted. For example, netting within categories of items that are netted for purposes of reporting to partners on Schedule K-1 pursuant to section 702 may be considered as appropriately netting.

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 part of the adjustment that results in a decrease in the amount of the imputed underpayment. For example, this rule could be implemented by disregarding the decrease in any item of income or gain and disregarding the increase in any item of deduction, loss, or credit.

Limitations that would apply at the direct or indirect partner level are treated as applying, unless otherwise determined. Under the provision, if an adjustment would decrease the imputed underpayment, and could be subject to a limitation or not be allowed against ordinary income if the adjustment were taken into account by any person, then the adjustment is not taken into account in determining the imputed underpayment of the partnership, except to the extent the Secretary otherwise provides.

For example, if an adjustment would increase the amount of a partnership loss allocable to partners, but the loss could be subject to the passive loss rule of section 469 in the hands of direct and indirect partners of the partnership, then the Secretary does not take into account the

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adjustment increasing the loss in determining the amount of the partnership's imputed underpayment, unless the Secretary provides otherwise. For example, the Secretary may provide otherwise if the partnership supplies accurate information that all direct and indirect partners of the partnership are publicly traded domestic C corporations not subject to the passive loss rule.

It is intended that an imputed underpayment may be modified under procedures described in section 6225(c).

Modifications to imputed underpayments (secs. 202, 203, and 206(b) of the bill and sec. 6225(c) of the Code)

The provision clarifies the modification rules of section 6225(c) to better carry out their function as intended by Congress, 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 efficient and prompt assessment and collection of tax attributable to the income of the partnership and partners.

The provision clarifies the procedures under section 6225(c)(2) that permit a partnership to seek modification of an imputed underpayment. These procedures allow reviewed-year partners to take adjustments into account so that the partnership's imputed underpayment can be determined by the Secretary without regard to that portion of the adjustments. Like other modification procedures in section 6225(c), these procedures take place within the period ending 270 days after the date the notice of proposed partnership adjustment is mailed, unless the period is extended with the consent of the Secretary, as provided in section 6225(c)(7).

Amended returns of partners

The provision clarifies the requirements for reviewed-year partners filing amended returns with payment of any tax due. First, the amended return procedure requires the partner to file returns for the taxable year of the partner that includes the end of the partnership's reviewed year, as well as for any taxable year with respect to which any tax attribute of the partner is affected by reason of any adjustment to a reviewed-year partnership-related item. Second, the amended returns are required to take into account all such adjustments that are properly allocable to the partner, as well as the effect of the adjustments on any tax attributes. Third, payment of any tax due is required to be included with the amended returns. If the requirements are satisfied, then the partnership's imputed underpayment amount is determined without regard to the portion of the adjustments taken into account by such partners. The amended return modification procedure applies with respect to tax paid with amended returns of direct partners of the partnership (not with respect to indirect partners). The amended return modification procedure does not require the participation of all direct reviewed year partners of the partnership. The amended return procedure is not intended to cover adjustments to items on an amended return of a partner that do not correspond to adjustments to a reviewed-year partnership-related item and the effect of the adjustments on tax attributes.

Alternative procedure to filing amended returns (pull-in)

The provision sets forth an alternative procedure to filing amended returns. The alternative procedure is referred to as the pull-in procedure. Under the pull-in procedure, the

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Secretary determines the partnership's imputed underpayment as reduced by the portion of the adjustments to partnership-related items which direct and indirect reviewed-year partners take into account and with respect to which those partners pay the tax due, provided the requirements of the pull-in procedure are met.

Under pull-in, reviewed-year partners pay the tax that would be due with amended returns, make binding changes to their tax attributes for subsequent years, and provide the Secretary with the information necessary to substantiate that the tax was correctly computed and paid. However, the partners file no amended returns. Thus, there are generally no corollary effects on the partners' returns beyond the effects on tax attributes, in subsequent years, of the adjustments to partnership-related items.

Pull-in is available generally to direct and indirect reviewed-year partners, in the case of tiered partnerships. More specifically, in the case of a partnership, any partner of which is a partnership, pull-in applies to any partner in the chain of ownership of the partnerships (treating an S corporation and its shareholders in the same manner as a partnership and its partners for this purpose). The pull-in procedure does not require the participation of all direct and indirect reviewed-year partners of the partnership.

Pull-in requires the participating partner to pay the tax that would be due under the amended return filing procedure. The partner is responsible for remitting the payment unless the Secretary provides that another person, such as the partnership or a third party, may remit the payment on the partner's behalf. Payment is due within the period ending 270 days after the date the notice of proposed partnership adjustment is mailed (unless the period is extended with the Secretary's consent). Pull-in requires that the effects on the partner's tax attributes of the adjustments to partnership-related items properly allocable to the partner are binding with respect to all subsequent taxable years of the partner (and binding on any successor to the tax attributes). Pull-in requires that the partner provide, in the form and manner specified by the Secretary, such information as the Secretary may require to carry out the provision. This requirement can include information in the same form as on an amended return, if the Secretary so specifies. The information is to be provided within the period ending 270 days after the date the notice of proposed partnership adjustment is mailed (unless the period is extended with the Secretary's consent). If all of the requirements are satisfied, the imputed underpayment can be modified. In the event that a partner provides the required information, but does not make the required payment, for example, the imputed underpayment of the partnership is not modified with respect to those adjustments.

For the administrative convenience of taxpayers and the Secretary, partner payments and partner information may be collected centrally and remitted to the Secretary under the pull-in procedure. This centralization could be administered by the Secretary, by the partnership representative, or by a third party. For example, the procedure may permit a third party such as an accounting or law firm designated by the partnership representative to collect partner information required under the procedure and tally partner payments before remitting this information to the Secretary. Such a practice may be useful both to facilitate centralized tracking and collection of the information and payments, and to address privacy concerns partners may have in sharing information with the partnership representative. Particularly in the case of partnerships with numerous partners or direct and indirect partners, such a practice may alleviate

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the administrative burdens on the Secretary and taxpayers, consistently with the Congressional intent for the centralized partnership audit system to improve the efficiency, promptness, and accuracy of collection of partners' taxes due with respect to partnership-related items.

Assessment authority with respect to payments under the pull-in procedure is provided under section 6201.

Rules applicable both to the amended returns of partners and to the pull-in procedure

If an adjustment involves reallocation of an item from one partner to another, the opportunity to modify the imputed underpayment under amended return procedure (sec. 6225(c)(2)(A)) or pull-in procedures (sec. 6225(c)(2)(B)) is available only if the requirements of one or the other of the amended return or pull-in procedures are satisfied with respect to all partners affected by the adjustment involving reallocation.

For purposes of the amended return and pull-in procedures, tax relating to adjustments to a reviewed-year partnership-related item and the effect of the adjustments on tax attributes may be determined and assessed without regard to the otherwise applicable statute of limitations of sections 6501 and 6511. For example, if a notice of proposed partnership adjustment is mailed to a partnership by the Secretary more than three years after a partner filed his or her return for the year including the end of the reviewed year, the three-year statute of limitations under section 6501 or 6511 does not preclude the filing of an amended return, the assessment and payment of the partner's tax due for that year, or the proper crediting or refund of an amount paid by a partner, but these results apply only with respect to adjustments to partnership-related items for the reviewed year (and the effect of such adjustments on any tax attributes).

Other modification procedures: adjustment not resulting in an imputed underpayment

The provision states specifically that the modification procedures are available if adjustments to partnership-related items do not result in an imputed underpayment. Under section 6225(c)(9), information relating to a modification may be offered by the partnership in the case of adjustments that do not result in an imputed underpayment, and such adjustments may be modified by the Secretary as the Secretary determines appropriate.

Push-out for passthrough partners in tiered structures (sec. 204 of the bill and sec. 6226 of the Code)

The provision addresses the situation of a partnership or an S corporation that is a direct or indirect partner of an audited partnership which has elected to push out adjustments of partnership-related items to partners under section 6226. The provision sets forth requirements applicable to such partners and the time frame for satisfying these requirements.

If a partner that receives a statement in a push-out is a partnership or S corporation, that partner must satisfy two requirements. First, the partner must file with the Secretary a partnership adjustment tracking report that includes information required by the Secretary. For example, the required information may include identifying the partner's own partners or shareholders, describing and quantifying adjustments necessary to determine partnership-related

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items or the equivalent in the hands of those partners or shareholders, or other information necessary or appropriate to assessment and collection from tiers of partners in a push-out.

Second, that partner is required either to pay its imputed underpayment under rules similar to section 6225, or to furnish statements to its partners or shareholders under rules similar to section 6226(a)(2). That is, the partnership or S corporation must either pay its imputed underpayment or push out the adjustments to its partners or shareholders. If such a partnership or S corporation chooses to pay its imputed underpayment, the rules of section 6225 apply (other than the modifications provided in section 6225(c)(2)(A) (amended returns), 6225(c)(6) (other procedures), 6225(c)(7) (270-day period for modifications), and 6225(c)(9) (modification of adjustment not resulting in imputed underpayment). The imputed underpayment of the partnership or S corporation is determined by appropriately netting all partnership adjustments on the statement (taking into account limitations to which adjustments that decrease the imputed underpayment could be subject) and applying the highest rate of tax in effect for the reviewed year under section 1 or 11, as provided in section 6225. The partnership or S corporation pays its imputed underpayment as so determined. However, the partnership or S corporation must push out the adjustments to its partners or shareholders (may not pay an imputed underpayment) if it elected out of the partnership audit regime for its taxable year that includes the end of the reviewed year of the audited partnership.

The due date for the filing of the partnership adjustment tracking report and for the payment of the imputed underpayment or furnishing of partner statements is the return due date (including extensions) for the taxable year of the audited partnership that includes the date of the final determination. That is, the partnership adjustment tracking report must be filed with the Secretary, and either the imputed underpayment paid or statements furnished to partners or S corporation shareholders, not later than the due date for the taxable year of the audited partnership that includes the date of the final determination with respect to the audited partnership. In the case of a partner that is not a partnership or an S corporation and that receives a statement in a push-out, the partner's tax is increased for the partner's taxable year that includes the date of the statement, as provided in section 6226(b).

The provision defines an audited partnership for purposes of the push-out treatment of passthrough partners in tiered structures under section 6226(b)(4). With respect to a partner that is a partnership or an S corporation and that receives a statement in a push-out, the audited partnership is the partnership in the chain of ownership originally electing the application of section 6226.

Failure of partnership to pay imputed underpayment (sec. 205 of the bill and sec. 6232 of the Code)

Under the provision, if, following an assessment, a partnership fails to pay an imputed underpayment within 10 days after the date of notice and demand by the Secretary, the applicable interest rate increases, and assessment and collection against adjustment-year partners for their proportionate shares may be made. The interest rate under the provision is the underpayment rate as modified, that is, the rate is the sum of the Federal short-term rate (determined monthly) plus 5 percentage points.

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The provision applies if, within 10 days of notice and demand for payment, a partnership fails to pay an imputed underpayment under section 6225 or any interest or penalties under section 6233, or a partner that is a partnership or S corporation in a push-out fails to pay an imputed underpayment under section 6226(b)(4)(A)(ii)(I) or any interest or penalties with respect to that amount. The S corporation and its shareholders are treated like a partnership and its partners for this purpose. The date of the notice and demand for payment initiates a two-year period in which the Secretary may assess against the adjustment-year partners.

If a partnership has ceased to exist or terminated (not including a technical termination) within the meaning of Code section 6241(7), it is intended that the provision apply with respect to the former partners of the partnership. For example, the former partners of the partnership may be the partners for the most recent period before the partnership ceased to exist or terminated.

A partner is liable for no more than the partner's proportionate share of the imputed underpayment, interest, and penalties, measured as the Secretary determines on the basis of the partner's distributive share of items under section 702. For example, the distributive shares set forth in the partnership agreement, or as determined for purposes of Schedule K-1, may serve as a measure of a partner's proportionate share. The Secretary is required to determine partners' proportionate shares so that the aggregate proportionate shares so determined total 100 percent. Thus, no partner is required to pay more than the partner's proportionate share of the imputed underpayment, interest, and penalties.

Partner payments reduce the partnership's liability to pay. The partnership's liability is not reduced by partner payments if such payments are made after the date on which the partnership pays, however. For example, if a partnership's liability is $100, and partner payments aggregating $60 before July 15 reduce the partnership's liability to $40, and the partnership pays $40 on July 15, a partner payment of $40 on August 1 does not reduce the partnership's liability. The partnership may not receive a credit or refund for any part of the partner payment of $40; the partner, however, may.

The Secretary may assess the tax, interest, and penalties on the proportionate share of each partner of the partnership as of the close of the adjustment year without regard to the deficiency procedures generally applicable to income tax.

Amendment of statements (Schedule K-1s) to partners (sec. 206(a) of the bill and sec. 6031(b) of the Code)

The provision clarifies that a partnership that has validly elected out of the partnership audit rules under section 6221(b), and therefore is not subject to the partnership audit rules, may amend partner statements (Schedule K-1s) after the due date of the partnership return to which the statements relate.

Partnership adjustment tracking report and administrative adjustment request not treated as amended return (sec. 206(b) of the bill and sec. 6225(c)(2) of the Code)

The provision clarifies that neither the partnership adjustment tracking report required to be filed in a push-out, nor an administrative adjustment request submitted under section 6227, is

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treated as a return for purposes of modifying an imputed underpayment of a partnership through partner amended return filings and payments under section 6225(c)(2)(A). Only a return of a partner satisfies the requirement under the partner amended return filing modification procedure.

Final determination with respect to partnership adjustment (sec. 206(c) of the bill and secs. 6225(d) and 6226(a)(2) of the Code)

The provision clarifies the time of a final determination with respect to a partnership adjustment. The final determination is made on the date the court decision becomes final (in the case of a court proceeding brought under Code section 6234), the date an administrative adjustment request is filed, or in any other case, the date that is 90 days after the date on which the notice of final partnership adjustment is mailed. The references in section 6227(b) to when an administrative adjustment request is made are conformed to refer to when it is filed. The provision does not alter the present-law period of limitation for filing an administrative adjustment request in 6227(c), generally providing a three-year limitations period and providing that in no event may a partnership file an administrative adjustment request after a notice of an administrative proceeding (i.e., the commencement of a partnership audit) with respect to the taxable year is mailed under section 6231(c).

The definition of the adjustment year is conformed to refer to the final determination. A conforming change clarifies that in a push-out under Code section 6226, statements to partners show the partner's share of any adjustment by reference to the final determination (not by reference to the notice of final partnership adjustment if it is not the final determination).

Assessment authority in a push-out (sec. 206(d) of the bill and sec. 6226 of the Code)

The provision clarifies that, in the case of a partnership that has validly elected under Code section 6226 (push-out) in the manner that the Secretary provides, no assessment of tax, levy, or proceeding in court for the collection of the imputed underpayment is to be made against the audited partnership.

Treatment of partnership adjustments that result in decrease in tax in push-out (sec. 206(e) of the bill and sec. 6226(b) of the Code)

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 partnership-related items as determined by reference to the final determination with respect to the adjustment. In this situation section 6225, requiring the audited partnership to pay the imputed underpayment, does not apply. Instead, each reviewed-year partner takes the adjustments into account for the taxable year that includes the date of the statement and pays the tax as provided in section 6226 (taking into account section 6226(b)(4)).

The provision provides that in taking into account adjustments to determine a partner's tax in a push-out, decreases as well as increases in the partner's tax are taken into account. The provision clarifies that the partner's tax for the taxable year that includes the date of the statement is adjusted by the aggregate of the correction amounts.

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The correction amount for a particular taxable year of a partner takes into account both decreases and increases. That is, the correction amount for the partner's taxable year that includes the end of the reviewed year is the amount by which the income tax would increase or decrease if the partner's share of adjustments were taken into account for that year. Similarly, the correction amount for any taxable year of the partner after that year, and before the year that includes the date of the statement, is the amount by which the income tax would increase or decrease if the partner's share of adjustments were taken into account for that year. The present-law treatment of mathematical or clerical errors applies with respect to correction amounts and aggregate correction amounts.

Time limit for notice of proposed partnership adjustment (sec. 206(f) of the bill and sec. 6231(b) of the Code)

The provision clarifies that a notice of proposed partnership adjustment must be mailed within the applicable period of limitations on making adjustments under the partnership audit rules (subchapter C of chapter 63 of the Code). The notice of proposed partnership adjustment cannot be relied upon to revive an otherwise expired limitations period under section 6235. For purposes of determining whether or not a notice of proposed partnership adjustment is timely, the applicable limitations period is determined under section 6235, determined without regard to section 6235(a)(2) (relating to the period for modification of an imputed underpayment under section 6225(c)(7)), and without regard to section 6235(a)(3) (relating to the 330-day period (or the period as extended) for making an adjustment after the date of a notice of proposed partnership adjustment).

The provision does not alter the section 6231(b)(2) prohibition against mailing any notice of final partnership adjustment earlier than 270 days after the date on which the notice of proposed partnership adjustment is mailed (except to the extent the partnership elects to waive the prohibition).

Deposit to suspend interest (sec. 206(g) of the bill and sec. 6233 of the Code)

The provision clarifies that, before the due date for payment of an imputed underpayment, a partnership (or, in the case of a partner payment pursuant to an election under section 6226, a partner) may make a cash deposit to suspend the running of interest as provided under present-law rules in section 6603. The deposit is not treated as a tax payment.

Treatment of special enforcement matters (sec. 206(h) of the bill and sec. 6241(10) of the Code)

The provision provides regulatory authority similar to that under the TEFRA partnership audit rules. It provides that in the case of partnership-related items involving special enforcement matters, the Secretary may prescribe guidance under which the partnership audit rules (or any portion of the rules) do not apply, and the special enforcement items are subject to special rules, including rules related to assessment and collection that are needed for effective and efficient enforcement. Special enforcement matters mean: failure to comply with the requirements of section 6226(b)(4)(A)(ii) to pay the imputed underpayment if the requirement to furnish statements has not been satisfied, termination and jeopardy assessments, criminal investigations,

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indirect methods of proof of income, foreign partnerships, and other matters presenting special enforcement considerations.

Penalties relating to administrative adjustment requests and partnership adjustment tracking reports (sec. 206(i) of the bill and secs. 6651, 6696, 6698, and 6702 of the Code)

The provision clarifies existing penalty provisions to ensure that they address compliance with the partnership audit rules. A partnership adjustment tracking report required to be filed pursuant to a section 6226 election is treated as a return for purposes of penalties relating to failure to file a partnership return, frivolous position submissions, and preparation of tax returns for other persons. A failure to comply with section 6226(b)(4)(A)(ii), relating to a push-out, is treated as a failure to pay for purposes of the penalty relating to failure to file a tax return or to pay tax. An administrative adjustment request under Code section 6227 is treated as a return for purposes of penalties relating to frivolous position submissions and the preparation of tax returns for other persons.

Statements to partners (adjusted schedules K-1) treated as payee statements (sec. 206(j) of the bill and sec. 6724 of the Code)

The provision clarifies that for purposes of the penalty for failure to furnish correct payee statements and the penalty for failure to file correct information returns, statements required to be furnished to partners in a push-out under Code section 6226(a)(2), or statements required to be furnished to partners under rules similar to section 6226(a)(2), are treated as payee statements. Statements required to be furnished to partners under rules similar to section 6226(a)(2) include statements furnished to partners pursuant to an administrative adjustment request under section 6227.

Clerical corrections relating to partnership audit rules (sec. 206(k) of the bill)

The provisions make clerical corrections to the partnership audit rules.

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C. Title III − Other Corrections

Amendments relating to the Bipartisan Budget Act of 2015

Electronic filing of partnership returns.–Present law requires that, under regulations, a person may be required to file returns electronically if the person is required to file at least 250 returns during the calendar year. Regulations provide that for purposes of determining the 250-return threshold, returns filed within one calendar year by a corporation include any type, including information returns (for example, Forms W-2, Forms 1099), income tax returns, employment tax returns, and excise tax returns. However, partnerships having more than 100 partners are required to file returns electronically. For partnerships only, the provision phases in reductions in the number of returns and statements during a calendar year that can subject the partnership to a regulatory requirement to file returns electronically. Specifically, the provision provides that under regulations, partnerships are required to file returns electronically if the partnership is required to file at least 200 returns for calendar year 2018, 150 returns for calendar year 2019, 100 returns for calendar year 2020, 50 returns for calendar year 2021, and 20 returns for calendar years after 2021. The provision is effective as if included with the partnership audit provisions of section 1101 of the Bipartisan Budget Act of 2015.

Amendments relating to the Energy Policy Act of 2005

Qualifying small power production facility (Act sec. 1253(b)(1)).–A provision of the MACRS depreciation rules, originally enacted in 1986 (Code sec. 168(e)(3)(B)(vi)(II)), refers to a provision of the Federal Power Act, as then in effect, defining a "qualifying small power production facility" as a facility that is "small" (power production capacity not greater than 80 megawatts) and not owned by an electric utility (as determined by FERC). The ownership limitation was repealed by the Energy Policy Act of 2005 (the "2005 Act"). Since that 2005 repeal, the determination is made by relying on FERC to determine whether a facility was a "qualifying small power production facility" as that term was defined prior to the 2005 Act, a determination no longer relevant to FERC (see, e.g., Private Letter Ruling 201539024). The provision adds to the Code the language of FERC's definition of a qualifying small power production facility (retaining the power production capacity not greater than 80 megawatts) without the electric utility ownership prohibition. The effect of the provision is that such a power production facility is 5-year property for purposes of Code section 168(e)(3)(B)(vi)(II), not 15-year property. The provision is effective for property placed in service after the date of enactment.

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D. Title IV − Clerical Corrections and Deadwood

Clerical corrections and deadwood-related provisions

The draft includes clerical corrections and deadwood-related provisions.

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