

The IRS has made major changes in the way they will audit partnership returns.

Under the new Bipartisan Budget Act that was passed on November 2, the IRS has made major changes in the way they will audit partnership returns. Before this law was passed, the IRS audited the partnership and then sent notices of administrative adjustments to each partner, which gives the partner his share of the assessment. This assessment will result in each partner amending his tax return for the audit year. Also, this resulted in an extremely time consuming task for the IRS, especially for large partnerships with more than 100 partners. Now, this procedure has been repealed effective for tax years beginning after December 31, 2017 (calendar years 2018 and forward). The partnership can make an election to be audited under the new procedures before January 1, 2018.

Under the new partnership audit rules, the IRS will assess the partnership the tax instead of each individual partner. The adjustments to income, deductions, etc. will be made in the year the partnership receives the notice of final partnership adjustment, not the year that was audited. However, the partnership can make an election within 45 days from the date of the final partnership adjustment to issue adjusted information returns to the partners that were partners in the year that was audited. These partners then can file through a simplified amended return process. The tax computation is equal to an "imputed underpayment", which is the net adjustment multiplied by the highest tax rate for corporations or individuals. However, partnerships may demonstrate that the underpayment would be lower if it were based on certain partner-level information and may pay that lower amount. This information could include amended returns of partners opting to file them, the tax rates applicable to specific types of partners and the type of income subject to the adjustments.

These rules also apply to limited liability companies that are classified as partnerships.