August 14, 2017

Via Federal eRulemaking Portal and U.S. Mail
CC:PA:LPD:PR (REG–136118–15), room 5207
Internal Revenue
P.O. Box 7604
Ben Franklin Station, Washington, DC 20044
Federal eRulemaking Portal: www.regulations.gov (SERVICE REG–136118–15).

Re: Rulemaking Comments by the Tax Section of The Florida Bar

Dear Sir or Madam:

I am pleased to submit The Florida Bar Tax Section's comments to the proposed regulations regarding implementation of section 1101 of the Bipartisan Budget Act of 2015, Pub. L. No. 114-74 (BBA), which was enacted into law on November 2, 2015, as corrected and clarified by the Protecting Americans from Tax Hikes Act of 2015, Pub. L. 114-113 div. Q (PATH Act). Section 1101 of the BBA repeals the current rules governing partnership audits and replaces them with a new centralized partnership audit regime that, in general, assesses and collects tax at the partnership level. These proposed regulations provide rules for partnerships subject to the new regime, including procedures for electing out of the centralized partnership audit regime, filing administrative adjustment requests, and the determination of amounts owed by the partnership or its partners attributable to adjustments that arise out of an examination of a partnership. The proposed regulations also address the scope of the centralized partnership audit regime and provide definitions and special rules that govern its application, including the designation of a partnership representative. The proposed regulations affect partnerships for taxable years beginning after December 31, 2017, and any partnerships that elect application of the centralized partnership audit regime pursuant to Temporary Regulation Section 301.9100–22T for taxable years beginning after November 2, 2015, and before January 1, 2018.

Principal responsibility for these comments was exercised by Gregory M. Marks, Mitchell Horowitz, Richard Alan Josepher, and Natalie A. Roberts. Although the members of the Florida Bar Tax Section who participated in preparing these comments may have clients who would be affected by the proposed regulations, no such member has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these comments.

Contact person:

Joseph Barry Schimmel, Esq.
Cohen, Chase, Hoffman & Schimmel, P.A.
9400 S Dadeland Blvd, Suite 600
Miami, FL 33156
Telephone 305-670-0201
Facsimile 305-670-6152
jschimmel@miamitaxlaw.com

As always, we will be pleased to provide additional commentary as requested. If you have any questions regarding our comments, please do not hesitate to contact us.

Sincerely,

Joseph Barry Schimmel

Digitally signed by Joseph Barry Schimmel
DN: cn=Joseph Barry Schimmel, o=Tax Section of The Florida Bar, ou, email=jschimmel@miamitaxlaw.com, c=US
Date: 2017.08.14 17:34:14 -04'00'

Joseph Barry Schimmel,
Chair, Tax Section of The Florida Bar

Comments to Proposed Regulations

Election Out for Certain Partnerships (Section 6221(b)[1] and Proposed Regulation Section 301.6221(b)-1[2])

1. Early Opt-in Election. Because of the short time frame for reviewing and becoming familiar with the new rules and guidance yet to be issued by the Internal Revenue Service (IRS), advising and making recommendations to partnerships as to the consequences of making or not making the elections available under the new rules, and in order to give partnerships a reasonable time to assemble the data necessary to make the determination of whether elections should be made, all existing partnerships should be given an opportunity to make the election for the new rules to apply to tax years beginning after November 2, 2015, and before January 1, 2018, within a reasonable time period following a notice of audit for those years (e.g., 45 days).

2. Opt-out Election/Eligible Partner Entities. For purposes of determining whether all of the partners of a partnership are eligible partners when making the opt-out election, no rational basis exists for distinguishing between an S corporation (which is a listed eligible entity) and certain other pass-through entities. There would appear to be no tax policy served by disqualifying these other entities, particularly when the Internal Revenue Code has recognized their deemed owners as the real taxpayer-in-interest for so many other purposes.

    a. The deemed owner of certain disregarded entities should be tested as an eligible partner for the purpose of determining opt-out eligibility of the partnership. This would apply for both determining how many K-1s are issued and the eligibility of the partner under the new rules. The disregarded entities would include a:
        i. Single owner limited liability company disregarded for income tax purposes and/or any disregarded entity as defined in Treasury Regulations Section 301.7701-2(c)(ii)[3];
        ii. Qualified subchapter S subsidiary; and a
        iii. Grantor trust.
            1. In the case of multiple grantors of a grantor trust, each would be treated as a single partner for the K-1 number test and meeting the number of partner test.
            2. At a minimum, a "single grantor" grantor trust should be eligible.
    b. The IRS could require a disregarded entity to provide the name, taxpayer identification number and any other applicable information with respect to its ultimate beneficial owner (the taxpayer-in-interest), so the IRS could determine whether this ultimate owner is an eligible partner for election out. The burden would fall upon the pass-through entity rather than the IRS. Because only one Schedule K-1 is required to be issued to a disregarded entity partner, only the ultimate taxpayer should be counted for purposes of the 100-or-fewer statements criterion.
    c. In addition, for purposes of determining whether the opt-out election can be made, upper-tier partnerships in certain multi-tiered partnership structures should be capable of being "collapsed." These "collapsed" structures are frequently required

for financing, licensing, franchising, liability management, development and other independent and legitimate business reasons. Sound tax policy would permit businesses to continue using these very common structures while permitting them to conduct tax audits at the ultimate beneficial owner level.

i. If the ultimate beneficial owners in the partnership structure are eligible partners (e.g., individuals, C or S corporations, or foreign entities that would be classified as corporations if they were domestic), then the partnerships included in that structure should be permitted to make an election, collectively, to opt-out of the centralized audit requirement.

ii. This election could be made in a single filing (or coordinated filings by all of the affected partnerships) to lessen any administrative complexity.

iii. The election for these multi-tier structures could be limited to situations where there are small and manageable numbers of beneficial owners (e.g., 10 or 20 ultimate eligible partners).

iv. As a practical matter, there would not be a significant difference in outcome between allowing a "collapse" or "look-through" election such as the one described above and the "push-out" election that can be made after the final adjustment. However, businesses and investors would be greatly benefited by the certainty of knowing in advance that the ultimate beneficial owners will be accountable for their net shares of the pass-through income and losses in the traditional manner (rather than the entities themselves).

v. Allowing all partnerships in such a multi-tiered structure to make the opt-out election and causing the ultimate owners to be identified in advance for audit purposes would have the same effect as allowing a push-out election to be made in advance. (See discussion regarding push-out below.)

vi. Because all of the tiered entities would be identified to the IRS in advance, along with the ultimate beneficial owners who would be the persons tested under the partner eligibility rules, the administrative burdens on the IRS would be considerably lessened.

d. At a minimum, second-tier partnerships having eligible partners should be treated the same as an S corporation for purposes of applying the eligible partner rules. In other words, a partnership (first tier) with a partnership (second tier) as one of its partners should be treated as an eligible partner of the first-tier partnership, so long as all partners of the second-tier partnership otherwise qualify as eligible partners (individuals, C or S corporations, etc.).

The same rules that apply for disregarding certain entities would apply at the second-tier partnership level in the same manner as if the entities were partners in the first-tier partnership.

i. For example: assume a partnership (first tier) has four partners: (A) an individual, (B) an S corporation, (C) a limited liability company disregarded for tax purposes that is owned by a C corporation, and (D) a limited liability company that is taxable as a partnership. Partner (D) (the second-tier partnership in this example) has three members: (E) a grantor trust, (F) an individual, and (G) another S corporation. Because all members of Partner (D) are eligible partners under the normal testing rules, (D) would qualify as an eligible partner of the first-tier partnership. Therefore, the first-tier partnership would be eligible to make the opt-out election. If a second-tier partner had been an ineligible entity, the first-tier partnership would not have been eligible to elect out of the centralized audit regime.

ii. Under the above example, the partners counted for purposes of the eligible partner test would be (A), (B), the C corporation owning (C), the grantor of (E), (F), and (G). The two S corporations would be subject to the normal rules governing the number of Schedules K-1.

3. De Facto Partnership Determinations. The preamble to the Proposed Regulations[4] states that the IRS intends to scrutinize whether two or more partnerships that have elected out should be recast as having formed one or more constructive or de facto partnerships for federal income tax purposes. The statement was made in connection with the IRS's self-proclaimed authority to disqualify the constituent "partners" in that kind of arrangement from making the opt-out election if they don't meet the tests on a combined basis. However, the IRS may also claim that a partnership exists among other persons who never had any intention of being classified as a partnership for income tax purposes, to assert the centralized audit procedures against those persons for administrative convenience.
    a. Because of the significant adverse consequences that could result from persons being treated as a partnership on an "after the fact" basis, we request the IRS to include some clearly defined standards, and corresponding safe harbors (if possible), in the final regulations to provide more certainty about how such authority would be applied.
    b. In addition, if a group of persons is determined to be a "partnership" for purposes of the new rules, that partnership should be given an opportunity within a reasonable period time after that determination (e.g., 45 days) to exercise the same elections afforded other partnerships under the rules, with appropriate election period adjustments to account for the fact that no prior return may have been filed (let alone a partnership tax year established for applying the election requirements).

Requirement that Partners' Returns be Consistent with Partnership Returns (Section 6222 and Proposed Regulation Section 301.6222-1)

1. Inconsistent Positions Properly Reported. Since the purpose of the proposed regulations is to further streamline the procedures to enhance IRS efficiency, the regulations should limit the ability of individual partners who identify an inconsistent treatment to receive an automatic right to contest the IRS's disagreement by utilizing the "normal" deficiency procedures under Section 6213(a).
    a. Proposed Regulation Section 301.6222-1(c)(4) provides that if a partner notifies the IRS of the inconsistent treatment of an item in accordance with the notification requirements, and the IRS disagrees with the inconsistent treatment, the IRS may adjust the identified item "in a proceeding with respect to the partner." Any such adjustment would be conducted pursuant to the deficiency procedures of Section 6213(a), which, in general, require issuance of a notice of deficiency prior to

assessment. This creates more activity in the audit process, and ultimately, in the Tax Court and is contrary to the objectives of the new system.

b. While the proposed regulations state that the IRS is not precluded from also conducting a separate partnership proceeding, it seems that the IRS would be required to conduct the partner proceeding pursuant to Section 6213(a). The proposed regulation should expressly state that if the IRS disagrees with the inconsistent treatment of the partner, but also determines that it will conduct a partnership proceeding, it may include the partner(s) who provided notice of inconsistent treatment. This would allow the IRS to avoid conducting separate partnership and partner proceedings. Time-frames would be provided within which the IRS must commence a partnership proceeding following the notice of inconsistent treatment. We suggest that proposed regulation Section 301.6222-1(c)(4) be revised to read as follows (see underline):

(4) Adjustment after notification--(i) In general. If a partner notifies the IRS of the inconsistent treatment of an item in accordance with paragraph (c)(1) of this section, and the IRS disagrees with the inconsistent treatment, the IRS may adjust the identified, inconsistently reported item in a proceeding with respect to the partner. Nothing in this paragraph (c)(4)(i) precludes the IRS from also conducting a proceeding with respect to the partnership. If the IRS determines that it will conduct a proceeding with respect to the partnership, the IRS may include the partner notifying it of the inconsistent treatment within the partnership proceeding and, in such case said partner is not entitled to contest the IRS determination under the deficiency procedures of subchapter B of chapter 63.

Partnership Representative (Section 6223(a))

1. Designation of Partnership Representative. The Partnership Representative (PR) has a tremendous amount of authority and discretion under the new rules.[5] The designation of this agent for that crucial role needs to be carried out very carefully and in accordance with the intent of the partners when their intent is evident, and in accordance with customary and established assumptions when it is not.
   a. The PR should be identified on at least an annual basis.
      i. Designation of the PR should be permitted in either the Form 1065, or at the election of the partnership, in a separate filing specifically for that purpose.
      ii. If the partnership decides to change the PR prior to filing the next annual tax return, it should be allowed to do so using the separate designation form.
   b. The currently-designated PR should have the sole authority to represent the partnership for all open years, including reviewed years when that PR may not have been acting in that capacity, because:
      i. The (current) adjustment-year partners will be primarily responsible for the assessed tax for the (prior) reviewed year, so they should have the ability to select the PR to represent the adjustment-year partnership for the audit.
         1. Using the PR who served during the reviewed year is not a workable convention because in many cases because that PR will no longer be

involved in the partnership's business and affairs. Also, no assumption can be made that the "former" PR's interests will be aligned with those of the adjustment-year partners who will bear the liability for additional taxes assessed for the reviewed year.

    ii. This same rationale should apply for selecting a PR when one has not been selected (or is not serving for other reasons). That is, the IRS should select an adjustment-year partner meeting the other criteria in the proposed regulations – but not a person who is no longer a partner, even if that person was a partner in the reviewed year.

  c. The final regulations should include a list of factors the IRS would consider in designating a PR. These factors should include the candidate's involvement in the partnership's business and affairs in addition to the factors currently listed in Proposed Regulation Section 301.6223-1(f)(5)(ii) (in which application of such factors is discretionary).
  d. A safe harbor should be established for determining whether the PR has a "substantial presence" in the United States.
    i. The "reasonably available" standard (and accompanying factors) as applied and determined solely by the IRS is not a certain and predictable yardstick for this purpose (and could potentially be very unfairly applied).
    ii. The tests used for determining when an individual is a resident alien (substantial presence) for filing purposes are inappropriate and are liable to be confused with the same nomenclature used in the proposed regulations.
    iii. The PR should be able to designate a location in the United States for purpose of communications between the PR and the IRS. The mechanics for designating such a location could operate in the same way that business organizations are required to designate a registered agent or other representative, and an address, for accepting service of process. The IRS would be entitled to rely upon that location until a new location is designated.
  e. If any disagreement occurs as to whether a person has the authority to serve as a PR for a partnership, the IRS should accept as conclusive a Notice of Removal of Partnership Representative (along with a designation of a successor PR), signed by all partners of the partnership.
    i. While this should not displace the other designation and resignation provisions in the final regulations, it would be a "fail stop" measure that would enable the partners to take precautionary steps to prevent a decision or other action during an audit that is wholly without authority of the partnership or at odds with the partners' mutual objectives.

<u>Partnership Adjustments (Section 6225 and Proposed Regulation Sections 301.6225-1, 301.6225-2)</u>

1. <u>Opportunity to Request a Hearing with the Appeals Office</u>. Section 6225 establishes time frames within which the partnership can seek modification of the imputed underpayment set forth in the Notice of Proposed Partnership Adjustment ("NOPPA"), file a Petition for

Readjustment once the Notice of Final Partnership Adjustment ("FPA") has been issued, or notify the IRS of an election to "push out" pursuant to Section 6226.

a. Modification - Within 60 days after the NOPPA has been issued, a partnership may request modification of the imputed underpayment. The statute and proposed regulations provide seven bases for modification. If none of these bases apply, a partnership's only recourse to contest an imputed underpayment is by filing a petition in Tax Court. The timeline created by the statute and proposed regulations affords no opportunity for the partnership to challenge the proposed adjustment by alternative means, such as requesting a hearing with the IRS's Appeals Office.

b. The proposed regulations should be revised to permit the opportunity to challenge, via the Appeals Office, the proposed audit adjustments prior to commencing the statutory modification process. This can be accomplished in one of two ways:

   i. Prior to issuing the NOPPA, the IRS could issue the equivalent of a 30-day letter, giving the partnership time to protest the adjustments and request a hearing with the Appeals Office. Appropriate extensions of the time should be in place to give Appeals sufficient opportunity to consider the issues. If Appeals agrees to readjust all or some of the protested items, the time and cost of the modification process could be avoided. Permitting such an appeals process would reduce the burden on the IRS and the time within which matters could be concluded.

   ii. Alternatively, within 30 days of the issuance of the NOPPA, the partnership could be permitted to "protest" the adjustments and request a hearing with the Appeals Office. The partnership and the IRS would agree to extend the 270-day period[6] in order to accommodate the time needed by Appeals to consider the issues and come to its determination. Again, if Appeals agrees with the protest letter, then the parties avoid the cost and time of going through the modification process.

In either case, if the Appeals Office does not agree with the partnership's position with respect to some or all of the issues, then the existing time frame re-commences (or the NOPPA is issued if the 30-day letter concept is used) and the partnership can pursue modification where appropriate. Alternatively, the statutory provision permitting the partnership to waive the 270-day period[7] should be preserved, because it serves to accelerate the issuance of the FPA in the event the partnership seeks to challenge it in Tax Court. This option once again permits both parties to avoid the time and cost of the modification process, while accelerating progress toward resolution.

2. <u>Tax Court's Ability to Consider Rejected Modification Requests</u>.

   a. Section 6234 provides for judicial review of partnership adjustments. An expansive reading of the statutory language suggests that the Tax Court has jurisdiction to consider rejected modification requests in determining the correct amount of any imputed underpayment. The final regulations should include explicit authorization for the Tax Court to consider and resolve modification issues.

b. In order to facilitate the Tax Court's ability to resolve issues in dispute, the final regulations should require the FPA to include not only the methodology used in determining adjustments and any imputed underpayment, but also an explanation of each modification requested by the partnership and rejected by IRS; detailed explanations such as these will enhance the Tax Court's ability to quickly assess the validity of the IRS's determination as to the imputed underpayment, if any, owed by the partnership.

Recommendations Regarding Election for an Alternative to Payment of the Imputed Underpayment ("Push-out") (Section 6226 and Proposed Regulation Sections 301.6226-1, 301.6226-2)

1. Tiered Partnerships. Once the FPA is issued, the 45-day clock begins to run for making the push-out election under Section 6226. The proposed regulations reserve on the issue whether the "push out" election should be limited to direct partners. Thus, a partner of a partnership, LLC, or "S" corporation that is itself a pass-through entity would have to pay the tax at the entity level, regardless of the fact that it is, itself, not normally a taxable entity and was not the subject of the audit in the first place. This is fundamentally wrong for a number of reasons.
   a. The economic arrangement among the ultimate taxable owners of the upper tier entities is that the owners, not the entities themselves, will bear the tax cost of the operations of the various tiered entities. This shifting of the burden will cause significant problems for these entities, particularly when frequent and substantial changes in ownership occur over the years.
   b. The concern that IRS cannot administratively trace through multiple tiers to the ultimate taxable owners is questionable. While the budgetary constraints under which IRS operates, and the manpower issues those constraints have caused, are appreciated, the burden of tracing could be transferred to the partnerships themselves.
   c. The proper treatment of adjustments and push-out payments by an "S" corporation under Section 1367 is not clear.
   d. The responsibility for payment should flow through to the ultimate taxpayer-in-interest. To accomplish this, the partnership should be allowed to "collapse" intermediate structures, as described above in the discussion regarding the election to opt out of the new regime. The final regulations should require the partnership being audited (the adjustment-year partnership) to provide all requisite information to the IRS at the time the push-out election is made, and for each tier in that structure to provide the same information within a certain time frame. If the information is not timely provided, then the event of taxation should terminate at that level. The mechanics could occur one of two ways:

i. Once the FPA is issued, the audited partnership has 45 days within which to make the push-out election. Assuming the partnership does not file a Tax Court petition, the adjustments become final 60 days after the 90-day period within which to file a petition expires, and the partnership then has another 60 days within which to issue the Section 6226 statements to its reviewed-year partners. As a copy of the initial push-out election is not required to be provided to these reviewed-year partners (it is only required to be filed with IRS), they may not know about the push-out election until receipt of the Section 6226 statements from the adjustment-year partnership, which occurs after the adjustments have become final. Reviewed-year partners which are themselves pass-through entities should have the ability to push out liability for the imputed underpayment to its own reviewed-year partners, who should have the ability to do the same. Each tier should have a period of time (say 45 to 60 days) in which to make its own push-out election, and provide its own statements to reviewed-year partners based on the statements received from the partnership below, on up the chain of tiers until a statement is received by an ultimate, taxable partner for the reviewed year. The final regulation should set a time certain, such as six months after the adjustments become final, by which all tiers must elect to push out and provide statements to its reviewed-year partners.

ii. Alternatively, at the time of the push-out election, the burden should rest upon the adjustment-year partnership to provide all necessary information to the IRS to allow the IRS to "collapse" all intermediate entities and identify the ultimate reviewed-year partners of the partnership. This would significantly and meaningfully increase the efficiency of partnership audits.

<u>Recommendations Concerning Accounting for Payment of Imputed Underpayments (Section 6241 and Proposed Regulations Sections 301.6225-4 and 301.6241-4)</u>

1. Section 6221 provides that any adjustment to "items of income, gain, loss, deduction, or credit of a partnership…any tax attributable thereto…and the applicability of any penalty…which relates to an adjustment to any such item or share or additional amount shall be determined at the partnership level pursuant to [the new, centralized audit regime]." Proposed Regulation Section 301.6241-4 provides that no deduction is allowed for any payment required to be made by a partnership under the new audit regime, and that payments, including interest, penalties, and other amounts are treated as an expenditure. Perhaps the most significant issue yet to be addressed is how adjustments and payments under the new rules will affect the outside basis and capital accounts of the responsible

partners, as well as the adjustment year partnership's tax and Section 704(b) "book" basis in its assets.[8] This provision in the proposed regulations has been reserved and comments have been requested.

2. Proper Tax Accounting. The Treasury has determined generally that the adjustment year partners' outside basis and capital accounts, and a partnership's basis in its property, should be adjusted to reflect what they would have been if the adjustments were made in the reviewed year, and should then be modified to account for how the adjustments would have affected taxes in intervening years. However, the IRS has not yet provided mechanical rules or methodologies for achieving appropriate results and has therefore requested public comments. Financial statements are typically prepared in accordance with Generally Accepted Accounting Principles; timely guidance for organizations that set accounting standards regarding proper tax accounting is critical and urgent. The final regulations should include methodologies and accounting rules for properly taking into account adjustments and payment of imputed underpayments in connection with partnership accounting, should address issues such as how to account for distinctions between capital and profits interest in allocating payments resulting from audits, whether there should be a default rule to honor existing partnership agreement allocation provisions negotiated by the parties, and how to properly account for intervening Section 754 elections. Safe harbors should be included. Accountants and taxpayers deserve to have advance notice of the IRS's accounting requirements, so as not to be caught in a "gotcha" administrative proceeding down the road. Further, all stakeholders will benefit from consistency in accounting rules and principles.

Conclusion

The Tax Section of The Florida Bar respectfully submits the above comments for consideration. We look forward to providing further input on the proposed regulations as needed.

---

[1] Unless otherwise indicated, all "Section" references are to the Internal Revenue Code of 1986, as amended (including amendments enacted under the BBA and the PATH Act).

[2] Preamble, IRS Proposed Rules (REG-136118-15, June 14, 2017) on Centralized Partnership Audit Regime, Notice of Sept. 18 Hearing, Withdrawal of Proposed Rules (REG-138326-07) ("Preamble").

[3] Treas. Reg. § 301.7701-2(c) Other Business Entities. — For federal tax purposes--

Treas. Reg. § 301.7701-2(c)(1) — The term partnership means a business entity that is not a corporation under paragraph (b) of this section and that has at least two members.

Treas. Reg. § 301.7701-2(c)(2) Wholly Owned Entities--

Treas. Reg. § 301.7701-2(c)(2)(i) In General. — Except as otherwise provided in this paragraph (c), a business entity that has a single owner and is not a corporation under paragraph (b) of this section is disregarded as an entity separate from its owner.

[4] Proposed Regulations, Preamble, Explanation of Provisions, Section 2.C.

[5] Section 6223(b).

[6] Prop. Reg. § 301.6225-2(c)(3)(ii).

[7] Prop. Reg. § 301.6225-2(c)(3)(iii)

[8] Preamble, Section 7.C.(i).