AMENDING LLC AND PARTNERSHIP AGREEMENTS FOR CHANGES IN PARTNERSHIP TAX AUDITS

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Effective as of tax years beginning in 2018, the rules for how the IRS audits companies taxed as partnerships will change dramatically. As many business owners may recall from reading client alerts and news articles over the past couple of years, the Bipartisan Budget Act of 2015 (the "BBA") (P.L. 114-74), repealed the existing partnership audit procedures under "TEFRA," which stands for the 1982 Tax Equity and Fiscal Responsibility Act, effective for tax years beginning in 2018.

Bipartisan Budget Act of 2015

The BBA provides that a new partnership tax audit regime (the "BBA Regime") will apply in IRS audits of partnerships for tax years in 2018 and thereafter. Owners of any company that is taxed as a partnership (including most LLCs, general partnerships, and limited partnerships) should review and possibly amend their operating agreement or partnership agreement to address the BBA Regime.

Some significant provisions of the BBA Regime that may be modified or addressed in the company's operating agreement or partnership agreement include the following:

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- Identifying a "partnership representative" who will have much authority on behalf of the partnership and the partners in the course of the audit. If a partnership representative is not designated by the company, the IRS has the power to designate one, and that person does not need to be an owner.
- Ensuring that the economic consequences of a partnership audit adjustment are borne by the proper parties. Any tax attributable to any adjustment of a partnership taxable year is determined, assessed, and collected at the partnership level (rather than the partner level) in the year of the adjustment. There are opportunities to elect out of the BBA or to push out the economic consequences to the owners of the company during the tax year that is the subject of the audit. These opportunities should be addressed in the company's operating agreement or partnership agreement.

Given that the BBA Regime is set to begin soon, now is the time to ensure that your operating agreement or partnership agreement contains all necessary provisions.

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