

BBA Tax Audits: Final Deadline for Designating a U.S. Partnership Representative

August 26, 2019

Key Points

- U.S. and non-U.S. investment funds that are required to file, or file, a U.S. partnership tax return (Internal Revenue Service (IRS) Form 1065) are generally subject to a new U.S. partnership audit regime that permits the IRS to assess and collect U.S. tax at the fund level.
- To comply with the new audit regime, funds that have yet to file their U.S. partnership tax return for the 2018 taxable year must designate a “partnership representative” (and its designated individual, if any) on such tax return no later than September 16, 2019 (October 15, 2019 for certain large electing partnerships).
- The partnership representative has the sole authority to act as the fund’s representative in the case of an audit and must have a “substantial U.S. presence.”

The U.S. Bipartisan Budget Act of 2015, as amended (BBA), significantly overhauled the audit regime applicable to U.S. and certain non-U.S. investment fund vehicles that are taxed as partnerships for U.S. federal income tax purposes. In general, under pre-existing audit rules, enacted under the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), adjustments are made in fund level audit proceedings, but flow through to the investors, and any associated tax must also be assessed by the IRS at the investor level. Under the BBA audit regime, which is generally effective for audits with respect to taxable years as of January 1, 2018, by default, any audit adjustment will be taxed at the fund level in the year of the adjustment, and investors are expected to indirectly bear the economic burden of any tax collected, regardless of whether they were investors in the fund in the reviewed year (i.e., the year that is under audit). The amount of fund level liability may be avoided if the fund is eligible for, and makes, a timely “push-out” election, which requires investors in the reviewed year to take into account the audit adjustment. Alternatively, the fund may seek to reduce the fund level liability for the adjustment year by demonstrating that certain investors in the reviewed year were subject to a lower rate of tax, qualified as a “tax-exempt partner,” paid any associated tax liability or reflected the audit adjustment in their tax attributes (which under a “pull-in” procedure may occur without filing an amended return). Similar rules may apply in states and localities for applicable tax audit purposes.

Contact Information

If you have any questions regarding this alert, please contact the Akin Gump lawyer with whom you usually work or

Patrick B. Fenn

Partner
pfenn@akingump.com
New York
+1 212.872.1040

Stuart E. Leblang

Partner
sleblang@akingump.com
New York
+1 212.872.1017

Lewis J. Kweit

Partner
lkweit@akingump.com
New York
+1 212.872.1041

Ron G. Nardini

Partner
rgnardini@akingump.com
New York
+1 212.872.1079

Olivier De Moor

Partner
odemoor@akingump.com
New York
+1 212.872.1032

Howard Leventhal

Senior Counsel
hleventhal@akingump.com
New York
+1 212.872.1099

Funds subject to the new audit regime must designate a “partnership representative” who, in a significant departure from prior law, has the sole authority to act vis-à-vis the IRS and to bind the fund and its investors upon audit. By default, the partnership representative is not required to keep investors informed or seek consent when making decisions. The fund’s partnership representative can be any person, including the fund itself or any unaffiliated third party, so long as such person has a “substantial presence” in the United States. This generally requires having a U.S. address, a U.S. telephone number, a U.S. taxpayer identification number and the ability to meet with the IRS in the United States at a reasonable time and place as determined by the IRS. If a fund designates a legal person as its partnership representative, then it must also designate a natural person (a “designated individual”) to act on behalf of such legal person, and such designated individual must meet the substantial U.S. presence requirement. If a fund fails to appoint a partnership representative, or the IRS determines that the fund’s designation is otherwise invalid (e.g., the partnership representative does not have a substantial U.S. presence), the IRS will generally notify the fund that it has 30 days to properly appoint a partnership representative and designated individual. If the fund does not timely take action, the IRS is authorized to make the relevant designations on the fund’s behalf.

Many fund managers have designated a management company, or a U.S. based affiliate or employee thereof, as the partnership representative or designated individual. Managers who do not have this option have sought to engage an external service provider as the fund’s partnership representative, specifically to address the need for a substantial U.S. presence. Managers who wish to appoint such service providers should carefully consider compliance with applicable regulations, including resignation and revocation procedures, as well as the impact of indemnities and other limitations under the fund’s governing documents and side letters.

Fund managers who have not yet filed their U.S. partnership tax return for the 2018 taxable year and have yet to determine their partnership representative (and, if applicable, designated individual) should do so expeditiously. The extended deadline for filing U.S. partnership tax returns is September 16, 2019. Funds who have elected to be treated as “electing large partnerships” have until October 15, 2019.

For additional information on this topic, see previous Akin Gump Tax Alerts [here](#) and [here](#).

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