News

New Income Tax Audit Regime – Partnership Agreements May Need to be Amended

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Partnerships or limited liability company ("LLC") agreements drafted before 2018 may need to be amended to address the new highly disadvantageous partnership income tax audit regime.

Historically, the IRS audits relatively few partnerships and LLCs because partnership tax is a conceptually difficult part of the income tax law, and because the partnership or LLC itself does not pay tax. Consequently, many of these partnership income tax audits result in deficiencies for some partners and offsetting refunds for other partners with a net revenue to the federal government of zero. This created little incentive for the IRS to audit partnerships.

Congress enacted a new audit regime for partnerships that treats partnerships more like corporations in order to enable IRS corporate auditors to be able to audit partnerships and to collect unpaid tax directly from the partnerships. Fortunately, many closely-held businesses can opt out of these partnership audit rules if no partner is itself a partnership or an irrevocable trust. Partnerships that cannot opt out of these new audit rules can still take action to minimize their harmful effects. Consequently, partnership or LLC agreements written before the end of 2017 may need to be updated to address these new partnership income tax audit rules.

If you have any questions or wish to discuss the above in greater detail, please contact Christopher Scott at 301-961-5135 or at cscott@linowes-law.com.