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The TEFRA Swamp: Managing the Complexities Of a Partnership Audit

By Sheri A. Dillon and Sam B. Guthrie[1]

While recent attention has focused on the challenges of auditing large partnerships, the same challenges pervade audits of small partnerships.[2] And though reform may be underway, the unified partnership audit and litigation procedures enacted in the Tax Equity and Fiscal Responsibility Act of 1982 (''TEFRA'')[3] may well apply to audits of partnership tax returns filed for tax year 2015, and possibly many subsequent years. In light of the lag time between filing a partnership tax return and commencing an audit, the IRS and taxpayers alike may find themselves grappling with the TEFRA procedures for longer than anyone would prefer. This article highlights some of the issues that can arise when navigating the TEFRA procedures, such as how to:

1. Recognize whether a partnership is subject to TEFRA;
2. Protect partners' notice and participation rights;
3. Understand the duties, powers, and limitations of the tax matters partner (''TMP'');
4. Distinguish partnership-level from partner-level items; and
5. Navigate the assessment process.

By shedding light on these issues, this article aims to help taxpayers and their representatives avoid unintended consequences in TEFRA proceedings. To fully appreciate the complexities of TEFRA audit issues, we begin with a brief description of the difficulties taxpayers faced before the enactment of TEFRA, and the problems TEFRA was intended to solve.

I. BACKGROUND

A. Pre-TEFRA Partnership Audits

Some of the challenges with partnership audits generally stem, however remotely, from a simple fact: partnerships do not pay federal income tax. Rather, ''a partnership is treated as a conduit through which income passes to its partners, who are then responsible for reporting any income or losses on their individual returns.''[4] Despite not paying tax, partnerships file informational tax returns — Forms 1065 — reflecting each partner's distributive share of partnership income, deductions, and credits. Until the enactment of TEFRA, the IRS could not make adjustments to items listed on Form 1065 at the partnership level. Rather, the IRS adjusted these partnership items just like partner-level items: through deficiency proceedings for each individual taxpayer, i.e., one taxpayer at a time.[5] The three-year period of limitations for assessment or refund was unique to each partner and began on the due date for each partner's tax return. Consistent with separate statutes of limitations, the IRS had to obtain consent from each individual partner to extend the period of limitations for assessment of partnership items. And if one partner reached a settlement with the IRS during audit, the settlement agreement did not bind the other partners. Similarly, a judicial

[1] Sheri A. Dillon is a partner at Vinson & Elkins, LLP, where she focuses her practice on resolving tax controversies. Sam B. Guthrie is a tax associate at Vinson & Elkins, LLP.

[2] The Government Accountability Office (''GAO'') defined ''large partnerships'' as those having 100 or more partners and $100 million or more in assets. *See* U.S. Gov't Accountability Office, GAO-14-732, *Large Partnerships: With Growing Number of Partnerships, IRS Needs to Improve Audit Efficiency* 1 (2014). We will use that same definition throughout this article, unless otherwise indicated.

[3] Pub. L. No. 97-248, 96 Stat. 324 (enacted Sept. 3, 1982) (enacting, among other provisions, §6221 through §6232 of the Internal Revenue Code). Unless otherwise noted, all references to ''§'' or ''Section'' and to ''the Code'' are to the Internal Revenue Code of 1986, as amended, and all references to ''Reg. §'' are to the Treasury regulations thereunder.

[4] *Prati v. United States*, 81 Fed. Cl. 422, 427 (2008), *aff'd*, 603 F.3d 1301 (Fed. Cir. 2010).

[5] *United States v. Woods*, 134 S. Ct. 557, 562 (2013).

determination relating to a partnership item bound only the parties to the proceeding. In short, partnership audits were fraught with fragmentation, duplicative efforts, and inconsistent results.[6]

B. The Promise of TEFRA: Unified Partnership Audits (and Lack Thereof)

Enter TEFRA. By enacting TEFRA in 1982, Congress sought to solve the problems that plagued partnership audits and litigation.[7] Specifically, Congress established unified procedures for determining tax treatment of partnership items at the partnership rather than the partner level.[8] These and other changes were intended to resolve partnership items in one consolidated proceeding rather than multiple partner-level proceedings, treat partners in the same partnership consistently — subject to individual partner rights — and achieve administrative and judicial efficiency by avoiding duplicative audits and litigation.[9] In sum, Congress sought to ease the IRS's administrative burden and enhance its ability to effectively audit partnerships, while simultaneously treating partners in the same partnership both fairly and consistently.[10] As discussed below, these efforts have met with varying degrees of success. Recently, though, TEFRA has come under fire for its shortcomings,[11] and tax scholars,[12] the Treasury Department,[13] Congress,[14] and the President[15] all have called for reform.

The data show that these calls for reform are well-founded. In three reports issued in 2014, the Government Accountability Office (''GAO'') identified numerous challenges in auditing large partnerships, and the inability of the IRS to overcome these challenges. In its March 19, 2014, report, the GAO determined that the IRS conducted field audits of less than 1% of partnerships with 100 or more partners and $100 million or more in assets (defined as ''large partnerships'') in 2011 and 2012.[16] In its July 22, 2014, report, the GAO noted that challenges in auditing large partnerships include the inability to timely identify the TMP, difficulty in passing through the adjustments to the ultimate taxpayers, and lack of timely reports from TEFRA specialists.[17] Finally, in its September 18, 2014, report (the ''September Report''), the GAO noted that the number of large partnerships has more than tripled since 2002 to over 10,000, and yet the IRS audits few large, complex partnerships compared to subchapter C-corporations.[18] Specifically, the September Report provided the following statistics, which reflected that a large corporation was over 30 times more likely to be audited than a large partnership in 2012:[19]

Fiscal Year	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Large Partnership Audit Rate	.5%	.6%	.6%	1.4%	.7%	.8%	N/A
Large Corporation Audit Rate	20.6%	21.4%	20.8%	20.6%	23.1%	27.1%	27.4%

[6] These problems came to a head in the late 1970s and early 1980s, when the use of pass-thru entities as tax shelters exploded. *See* Steve R. Johnson, *Reforming Federal Tax Litigation: An Agenda*, 41 Fla. St. U. L. Rev. 205, 232 n. 202 (2013) (''For example, between fiscal years 1978 and 1986, largely because of tax shelters, the number of petitions pending in the Tax Court rose from 23,140 to 83,686. The total rose each year and often dramatically. The 1979 increase was 16.9% followed by a 28.9% increase in 1980 and a 31.7% increase in 1981. . . . Tax shelter petitions were the main drivers of these increases.'') (internal citation omitted).

[7] *See* Staff of Joint Comm. on Taxation, 97th Cong., General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982, No. JCS-38-82, at 268 (Joint Comm. Print 1982).

[8] *Id.*

[9] *See Woods*, 134 S. Ct. at 562–63.

[10] *See* Johnson, n. 6 above, at 233 (''Manifold purposes were at work in the creation of the TEFRA partnership regime. The main inspiration, of course, was protecting the revenue by providing a more workable method for auditing tax shelters.'').

[11] *Tigers Eye Trading, LLC v. Commissioner*, 138 T.C. 67, 92 (2012) (''The substantive and procedural rules applicable to the income taxation of partners and partnerships are 'distressingly complex and confusing.' '') (quoting *Rhone-Poulenc Surfactants & Specialties, L.P. v. Commissioner*, 114 T.C. 533, 539–40 (2000)).

[12] N. Jerold Cohen and William E. Sheumaker, *When It's Broke, Fix It! It's Time for TEFRA Reform*, 2012 Tax Notes Today 157-2 (Aug. 13, 2012); Peter A. Prescott, *Jumping the Shark: The Case for Repealing the TEFRA Partnership Audit Rules*, 11 Fla. Tax Rev. 503 (2011).

[13] Treasury Inspector Gen. for Tax Admin., No. 2014-30-082, *Improvements Are Needed to Ensure That Procedures Are Followed During Partnership Audits Subject to the Tax Equity and Fiscal Responsibility Act of 1982* (2014).

[14] Partnership Auditing Fairness Act, S. 3018, 113th Cong. (2014); Tax Reform Act of 2014, H.R. 1, 113th Cong. (2014).

[15] Office of Mgmt. & Budget, Exec. Office of the President, *Fiscal Year 2015: Budget of the U.S. Government* 192 (2014).

[16] U.S. Gov't Accountability Office, GAO-14-379R, *Large Partnerships: Characteristics of Population and IRS Audits* 20 (2014).

[17] U.S. Gov't Accountability Office, GAO-14-746T, *Large Partnerships: Growing Population and Complexity Hinder Effective IRS Audits* 15 (2014).

[18] U.S. Gov't Accountability Office, GAO-14-732, n. 2 above, at 13.

[19] *Id.* at 20. 2012 was the most recent year for which data were available.

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The September Report also provided data reflecting that even when the IRS does audit large partnerships, unlike in its audits of large corporations, the IRS generally does not make adjustments to partnership income:[20]

[20] *Id.* at 21.

Fiscal Year	2007	2008	2009	2010	2011	2012	2013
Large Partnership No Change Rate	85.3%	77.8%	82.6%	51.6%	77.0%	66.7%	64.2%
Large Corporation No Change Rate	16.2%	22.1%	18.6%	18.7%	20.4%	27.2%	21.4%

The GAO's statistics show that the IRS both (1) audits large corporations much more frequently than large partnerships, and (2) is more effective in auditing large corporations than large partnerships.

Despite the recent furor over low audit rates for large partnerships, though, the *IRS Data Book, 2014* suggests that the low partnership audit rate is not unique to large partnerships. In fiscal year 2014, for example, the IRS examined just .4% of all partnership returns filed in calendar year 2013.[21] It is likely that the low partnership audit rate is a consequence, at least in part, of the complexities of TEFRA and the significant resources and time that TEFRA partnership audits require. As discussed below, where TEFRA does fall short or is overly complex, its shortcomings and complexities often inure to the benefit of the IRS, and certainly do not benefit the unwary partner. For that reason, partners in all partnerships should be mindful of the scope and intricacies of TEFRA.

II. REALITIES OF TEFRA: CHALLENGES WITH TEFRA PARTNERSHIP AUDITS

A. Partnerships Subject to TEFRA

While not all partnership audits are subject to the TEFRA procedures, more partnerships may be subject to TEFRA than one would expect.[22] In general, TEFRA applies to any entity that is required to file a partnership return.[23] However, TEFRA excepts from its reach what it defines as ''small partnerships.''[24] A ''small partnership'' is any partnership having 10 or fewer partners, each of whom is an individual, a C corporation, or an estate of a deceased partner.[25] While at first blush this may appear to be a simple rule, many partnerships one might think of as ''small'' are in fact subject to the TEFRA procedures. This is because the applicability of the small partnership exception depends not only on the number of partners, but also on the classification of partners in the partnership. For example, the small partnership exception will not apply if any partner is a ''pass-thru partner,'' such as an S corporation, another partnership, or a trust.[26]

Taxpayers are often surprised to find that even disregarded entities, such as grantor trusts, are not disregarded for this purpose. Thus, if a partnership has an individual partner who holds his interest through a grantor trust, the partnership cannot qualify for the small partnership exception and will be subject to TEFRA.[27] Likewise, if a partnership includes a single-member LLC (''SMLLC''), which is disregarded as an entity separate from its owner under the check-the-box regulations, the IRS has nevertheless ruled that the partnership is subject to TEFRA.[28] In Rev. Rul. 2004-88, the IRS concluded that TEFRA applied to a partnership of five partners, of which four were individuals and one was an SMLLC disregarded from its owner for tax purposes. Applying state law principles, the Service determined the SMLLC, while a disregarded entity for federal tax purposes, was a pass-thru partner under §6231(a)(9). Consequently, because the partnership had a pass-thru partner, SMLLC, the small partnership exception to the TEFRA partnership provisions did not apply to the partnership. This conclusion seemingly is inconsistent with the check-the-box regulations, which provide that a disregarded entity's activities ''are treated in the same manner as a sole proprietorship, branch, or divi-

[21] Internal Revenue Serv., Dep't of the Treasury, *Internal Revenue Service Data Book, 2014* 23 table 9a (Pub. 55B 2015). Data from calendar year 2013 are presented because, in general, examination activity is associated with returns filed in the previous calendar year.

[22] *See, e.g., Bedrosian v. Commissioner*, 143 T.C. No. 4 at *14 (2014) (''It can even be complex and confusing to determine whether a partnership is subject to TEFRA.'').

[23] §6231(a). A limited liability company that elects to be treated as a partnership and files a partnership tax return, therefore, can be subject to TEFRA, unless it qualifies as a ''small partnership.''

[24] §6231(a).

[25] §6231(a)(1)(B)(i). For this purpose, a husband and wife (and their estate) are treated as one partner.

[26] §6231(a)(9).

[27] This could be particularly relevant for estate planning partnerships, where grantor trusts are often partners.

[28] *See* Rev. Rul. 2004-88, 2004-2 C.B. 165. *See also 6611, Ltd. v. Commissioner*, T.C. Memo 2013-49; *Tigers Eye Trading, LLC v. Commissioner*, T.C. Memo 2009-121. This could be particularly relevant for real estate development partnerships, where developers often form single-member LLCs to hold their partnership interests.

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sion of the owner,''[29] and thus may catch taxpayers off guard.

For example, suppose that a partnership with three partners (two individuals and one SMLLC) has interest expense (a partnership item) to report on its Form 1065 and Schedules K-1. Also suppose that the partnership inadvertently omits the interest expense from its partnership return. One of the individual partners (''Partner I'') realizes the error and, during an audit of Partner I's tax return, makes an affirmative claim to adjust the interest expense reported on her return, as her period of limitations for assessment is open. Partner I mistakenly believes that the partnership is not a TEFRA partnership because it has fewer than 10 partners. Upon review of Partner I's claim, the IRS determines that the partnership is in fact a TEFRA partnership because it has a pass-thru partner, and the TEFRA partnership's statute of limitations is closed. Accordingly, Partner I's claim is time-barred, because the interest expense is a TEFRA partnership item that could only be adjusted in a TEFRA proceeding.[30]

In addition, partnerships that might not otherwise be subject to the TEFRA procedures, such as small partnerships, may still be subject to TEFRA if the IRS reasonably determines that the TEFRA rules apply to that partnership based on its review of the partnership's tax return.[31] That is to say, the IRS's review of the partnership return itself is determinative of whether TEFRA in fact applies. If, on the basis of the face of the partnership return, the IRS reasonably determines that the TEFRA rules should apply, then those rules apply, even if the IRS's determination is in error.[32] Conversely, if the IRS reasonably determines that the TEFRA rules should not apply, even if it does so erroneously, the TEFRA rules do not apply, and deficiency proceedings apply instead.[33] Until recently, there was little guidance as to the meaning of ''reasonably determines,'' leaving considerable discretion to the IRS.

In *Bedrosian v. Commissioner*,[34] the Tax Court noted this lack of authority as it sought to apply the ''reasonably determines'' standard: ''There is no indication that Congress intended the term 'reasonable' to have any specific meaning, and so we give it its ordinary meaning.''[35] To do so, the court first consulted multiple dictionary definitions of ''reasonable'' and concluded that the general dictionary definitions are ''not inconsistent with the use of the term 'reasonable' elsewhere in the Code.''[36] The court then concluded that the use of the term ''reasonable'' in §6231(g) was most analogous to the use of the phrase ''reasonable basis'' in Reg. §1.6662-3(b)(3) because determining whether TEFRA applies to a particular partnership based on the information shown on the face of a partnership return is similar to determining whether a reasonable basis exists for a position reported on a tax return.[37] The court then quoted the reasonable basis standard in full, and ''[a]gainst this backdrop,'' analyzed whether the IRS could have reasonably determined that TEFRA applied to the partnership at issue.[38] The partnership at issue had filed a Form 1065 with conflicting information. On the one hand, the partnership ''expressly reported that it was not subject to the TEFRA procedures by answering 'no' to the question. . .which asks: 'Is this partnership subject to the consolidated audit procedures of section 6221 through 6233? If ''Yes,'' see Designation of Tax Matters Partner below.' ''[39] On the other hand, the partnership designated a TMP.[40] Additionally, one of the Schedules K-1 included with the partnership return listed an LLC as a partner, and another listed an S corporation as a partner.[41]

Notwithstanding the partnership's inconsistent responses to questions on the return, the *Bedrosian* court held that it would have been unreasonable for the IRS to determine that the partnership was not subject to the TEFRA procedures.[42] Focusing on the Schedules K-1 that listed an LLC and an S corporation as partners, the court concluded that ''the presence of any passthrough partner precludes the application of the small partnership exception and. . .renders the partnership subject to TEFRA as a matter of law. Relying on the face of the partnership return, the only reasonable conclusion is that TEFRA applies to the [partnership].''[43] In other words, the IRS's determination that TEFRA does not apply is unreasonable if, based on information stated on the face of the return, TEFRA would apply *as a matter of law*. However, had the Schedules K-1 not reflected the presence of pass-thru partners, it remains unclear how the *Bedrosian* court would have ruled, given the conflicting information otherwise provided on the return. Accordingly, while *Bedrosian* provides some guidance as to what would constitute an ''unreasonable'' determina-

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[29] Reg. §301.7701-2(a).

[30] *Cf. Brumbaugh v. Commissioner*, T.C. Memo 2015-65. See also the discussion below at II.C.2.

[31] §6231(g).

[32] §6231(g)(1).

[33] §6231(g)(2).

[34] 143 T.C. No. 4 (2014).

[35] *Id.* at *18.

[36] *Id.* at *19.

[37] *Id.*

[38] *Id.*

[39] *Id.*

[40] *Id.*

[41] *Id.* at *20.

[42] *Id.*

[43] *Id.*

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tion based on the face of the return, the meaning of a "reasonable" determination remains unclear.

In sum, partners should not assume that they are exempt from the TEFRA procedures simply because their partnership has few partners and limited assets. In particular, partners should be mindful that the small partnership exception does not apply if the partnership has any pass-thru partners, e.g., entities such as SMLLCs and grantor trusts, which are otherwise disregarded for federal income tax purposes. Thus, what might intuitively seem to be a small partnership may still be subject to TEFRA. Moreover, TEFRA applies to *any* partnership if the IRS reasonably determines that it should apply on the basis of the partnership return, even if the IRS's determination is in error. All partners, therefore, should be particularly aware of the TEFRA procedural rules and be meticulous in completing the partnership return, lest they forfeit their rights to challenge IRS adjustments to partnership items. As the Tax Court noted in *Bedrosian*, "Congress' goal in enacting section 6231(g) was *to simplify the IRS's task* of choosing between the TEFRA procedures and the normal deficiency procedures by permitting the IRS to rely on a partnership's return."[44] This is but one example demonstrating that the TEFRA procedures were designed predominantly to benefit the IRS.

B. Partners

All partners, including indirect partners, are subject to the TEFRA proceedings of the source partnership and have the right to participate in the proceedings. Exercising participation rights can be difficult in practice, however, as not all partners have the right to notice from the IRS. And, the notice that the IRS is required to provide to those partners entitled to notice, referred to as "notice partners," is quite limited.[45] Rather, when enacting TEFRA, Congress provided the IRS a liaison, the TMP, to serve as the IRS's primary point of contact with the partnership. The TMP thus plays a crucial role in the partnership administrative proceedings and any resulting judicial proceedings. Concomitantly, the TMP has expanded rights and duties compared to other partners. In particular, it is the responsibility of the TMP to keep the other partners informed of partnership proceedings. As explained below, among other powers, the TMP has the authority to extend the statute of limitations for all partners and limited settlement authority with respect to adjustments to partnership items. While the TMP's role in TEFRA proceedings lightens the IRS's administrative load, shifting what are thought of as uniquely government responsibilities — administration of the tax law and apprising taxpayers of the IRS's actions — may have adverse consequences for those partners reliant on the TMP.

1. Classification of Partners

For purposes of TEFRA, a partner includes "a partner in a partnership" and "any other person whose income tax liability under subtitle A is determined in whole or in part by taking into account directly or indirectly partnership items of the partnership."[46] As the statutory definition implies, partners are either direct or indirect partners. An indirect partner is a person who holds an interest in a partnership through one or more pass-thru partners.[47] A pass-thru partner, in turn, is "a partnership, estate, trust, S corporation, nominee, or other similar person through whom other persons hold an interest in the partnership."[48] For partnerships with 100 or fewer partners (including indirect partners), all partners are notice partners.[49] For partnerships with more than 100 partners, only partners with a 1% or more profits interest are notice partners.[50] Therefore, partners who have less than a 1% profits interest in a partnership with more than 100 partners are generally non-notice partners.

Recognizing that non-notice partners may nevertheless desire notice more directly from the IRS (so as not to be reliant on the TMP for all information), TEFRA provides that partners who each have a less than one percent interest, but collectively have a five percent or greater interest, may band together to form a "five percent group" by filing a statement with the IRS.[51] A five percent group is essentially treated as a notice partner, and TEFRA requires the IRS to provide notice of NBAPs and FPAAs to a designated representative of the notice group.[52] TEFRA also provides a special rule for indirect partners who desire notice from the IRS; any indirect partner whose name, address, and profits interest is timely furnished to the IRS, is treated as a notice partner.[53]

[44] *Id.* at *15 (emphasis added).

[45] As discussed more fully below, the IRS is only required to provide notice partners two types of notice: notice of the beginning of administrative partnership proceedings ("NBAPs") and of the completion of administrative proceedings, reflected in the final partnership administrative adjustment ("FPAAs"). §6223(a).

[46] §6231(a)(2).

[47] §6231(a)(10).

[48] §6231(a)(9).

[49] §6223(a).

[50] §6223(b)(1).

[51] §6223(b)(2).

[52] *Id.*

[53] §6223(c)(3).

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2. Notice Provided by the IRS

The IRS is required to inform all notice partners of the beginning of a partnership audit and any final partnership adjustments.[54] TEFRA provides that the IRS must first mail an NBAP to the TMP and notice partners no later than the 120th day before the day on which the FPAA is mailed (the ''120-day rule'').[55] The Treasury Regulations further provide that the IRS may withdraw the NBAP to the TMP within 45 days of issuing it, and if the IRS does so, ''neither the Internal Revenue Service nor the tax matters partner is required to furnish any notice with respect to that proceeding to any other partner'' (the ''45-day rule'').[56] Finally, the Treasury Regulations clarify that ''[e]ven if the Internal Revenue Service does not withdraw the [NBAP], the Internal Revenue Service is not required to issue [an FPAA].'' In sum, TEFRA and the regulations thereunder (1) require the IRS to issue an NBAP at least 120 days before an FPAA;[57] (2) allow the IRS to withdraw an NBAP within 45 days of issuance and thereby avoid providing notice of a TEFRA audit to notice partners; and (3) explain that even if the IRS does not withdraw an NBAP, the IRS does not necessarily have to issue an FPAA.[58] Nowhere do the Code or Treasury Regulations suggest that the IRS does not have to issue NBAPs; to the contrary, §6223(a)(1) unequivocally requires the IRS to send NBAPs to notice partners.[59]

In recent chief counsel advice (''CCA''), however, the IRS concluded that if it ultimately determines not to issue an FPAA, it may *completely forgo* issuing NBAPs to notice partners throughout the course of the TEFRA partnership audit.[60] In other words, the IRS has taken the position that the 120-day rule determines *whether* the IRS must issue an NBAP, as opposed to *when* the IRS must issue an NBAP. Citing the 45-day rule, which states that the IRS does not always have to issue an FPAA, the CCA concludes that the 120-day rule requires the issuance of NBAPs to notice partners only if the IRS ''ultimately issues an FPAA to the TMP.''[61] Not only does the CCA fail to address the notice requirement set forth in §6223(a), it erroneously (and illogically) treats the rule setting forth the time period within which the NBAP notice must be mailed (the 120-day rule) as an exception to the NBAP requirement altogether. Effectively, the IRS has interpreted the 120-day rule (which is intended to provide redress to partners whose participation rights in an administrative proceeding may be impaired due to a failure to receive timely notice) as a means to avoid providing notice at all. The CCA's conclusion, however, cannot be reconciled with a partner's ''right to participate in any administrative proceeding relating to the determination of partnership items at the partnership level.''[62] The CCA undermines Congress's intent, clearly embodied in §6224(a), to provide partners participation rights in partnership proceedings, by depriving partners of the very notice necessary to even begin participating.[63]

At first glance, the distinction between notice partners and non-notice partners may appear to be a fine one. After all, the TMP is required by statute to provide notice of administrative and judicial proceedings to non-notice partners. Furthermore, the IRS is only required to provide NBAPs and FPAAs to notice partners; thus notice and non-notice partners alike are generally reliant on the TMP for the relevant information necessary to exercise their participation rights.[64] Nevertheless, as discussed below, if the TMP fails to furnish an NBAP or FPAA to its non-notice partners, the prejudiced partners may be left with little recourse in their proceedings with the IRS. The non-notice partners may not even be aware a partnership proceeding is ongoing, much less be aware of their rights

[54] §6223(a).

[55] *Id.*; §6223(d)(1). Additionally, the IRS must mail the FPAA to all notice partners no later than 60 days after it mails the FPAA to the TMP. §6223(d)(2).

[56] Reg. §301.6223(a)-2(a).

[57] §6223(d)(1).

[58] Reg. §301.6223(a)-2(a).

[59] One might argue this technically is not a requirement, because §6223(a)(2) similarly ''requires'' the IRS to issue notices of FPAAs resulting from administrative proceedings, but §301.6223(a)-2(a) states that the IRS is *not* required to issue a notice of FPAA. However, not all partnership proceedings result in administrative adjustments, whereas every partnership proceeding has a beginning (and thus requires an NBAP).

[60] *See* PMTA 2014-06 (May 9, 2014).

[61] *Id.* at 2.

[62] §6224(a). *See* Johnson, n. 6 above, at 233 (concluding that, rather than imposing an entity-based system to achieve maximum administrative efficiency, ''Congress chose. . .to impose a hybrid system including substantial notice and participation rights for partners as an essential part of the bargain. Thus, even in this context, Congress cared a lot about providing procedural options that were fair to taxpayers and perceived by them to be fair.'' (footnote omitted)).

[63] This point is most evident when considering what happens when the IRS *does* issue an FPAA at the conclusion of the TEFRA proceeding. Suppose, for example, that the IRS opens an audit of a partnership's 2013 tax return on June 1, 2015, and mails the TMP an NBAP on that date. Suppose further that the IRS discovers significant issues with the tax reporting of partnership items and audits these issues for two years. Ultimately, in June 2017, the IRS determines that it will make adjustments to the partnership's items by issuing an FPAA. In this scenario, under the IRS's interpretation of §6223, it simply needs to mail the NBAPs first to the notice partners, and then mail the FPAA 120 days later to the TMP. Obviously, the IRS has made its determinations and the purported notice partners had no opportunity to participate in the TEFRA proceeding.

[64] §6223(g).

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to participate.[65] Additionally, the TMP plays a critical role in settlement discussions and litigation. In many instances where the TMP makes an unfavorable decision or breaches a statutory duty, notice partners' statutory rights are superior to those of non-notice partners.

3. Notice Provided by the TMP

The TMP's powers are perhaps best illustrated by the TMP's relationship with non-notice partners. For non-notice partners, the TMP, rather than the IRS, is responsible for informing the partners of every aspect of the partnership proceedings, including mailing copies of the NBAP[66] and FPAA.[67] In addition, the TMP must provide information to notice and non-notice partners of various other events during the administrative proceedings: a closing conference with examining agents; proposed adjustments, rights of appeal, and requirements for filing of a protest; the time and place of any Appeals conference; acceptance by the IRS of any settlement offer; consent to the extension of the partnership statute of limitations; the filing of a request for administrative adjustment; the filing by any partner of a petition for judicial review under §6226 or §6228(a); the filing of any appeal of any judicial determination provided for in §6226 or §6228(a); and final judicial redetermination.[68] Under the regulations, the TMP ''shall'' provide the above notices within 30 days of taking the action or receiving the information that necessitates notice.[69]

In this instance, however, ''shall'' is a relative term. Despite the regulations' 30-day requirement, neither notice nor non-notice partners have any statutory remedy if the TMP fails to provide any of these notices. Thus, a partner's ability to participate in partnership proceedings is highly dependent on the TMP timely performing its notice responsibilities. At best, if a partner is prejudiced by a lack of notice, then the partner might have a private right of action against the TMP. In many cases, though, that may be little consolation for the prejudice suffered in the government proceeding. Partners should thus be careful in designating a TMP, or, better yet, specify the TMP's notice (and as discussed below, other) duties in the partnership agreement and include contractual liability for breach of those duties.

4. The TMP's Authority

The partners should also be wary of the TMP's powers to act for the partnership. For example, the TMP may extend the statute of limitations,[70] file suit,[71] and file a refund claim or substitute tax return[72] on behalf of the partnership. Furthermore, the TMP may bind a non-notice partner[73] to any settlement negotiated with the IRS during the administrative level of the TEFRA proceeding, unless the non-notice partner specifically notifies the IRS that it does not wish to be bound by the TMP.[74]

Because the TMP has such significant rights and responsibilities, and because the IRS must rely on the TMP's authority, TEFRA limits which partner may be designated the TMP. As an initial matter, the TMP must be a partner with the authority to bind the partnership; otherwise, any agreements executed by the TMP on behalf of the partnership, such as a Form 872-P, *Consent to Extend the Time to Assess Tax Attributable to Partnership Items*, or a settlement agreement, would not be enforceable. This is why the IRS spends a significant portion of its resources ensuring that the TMP is properly designated. For example, a general partnership may designate any partner with a profits interest who was a partner during the year for which the designation was made or at the time of the designation.[75] A limited partnership may only designate a general partner as the TMP.[76] An LLC may designate the managing member,[77] but if the LLC does not have a managing member, then any member will do.[78] In all cases, however, if a United States partner is eligible under the regulations to serve as TMP, then a foreign partner cannot serve as the TMP without the consent of the IRS.[79]

The partners designate a TMP, on a yearly basis, on the partnership return for each taxable year.[80] If the partnership does not designate a TMP, the general

[65] And, to the extent that the IRS follows the Chief Counsel's advice to program managers discussed at n. 60 above and the accompanying text, notice partners would face the same problem.

[66] Within 75 days after the IRS mails an NBAP, the TMP must forward a copy of the NBAP to non-notice partners.

[67] Within 60 days after the IRS mails an FPAA, the TMP must forward a copy of the FPAA to non-notice partners.

[68] Reg. §301.6223(g)-1(b)(1)(i)–§301.6223(g)-1(b)(1)(ix).

[69] Reg. §301.6223(g)-1(b)(3).

[70] §6229(b)(1)(B).

[71] §6226(a).

[72] §6227(c).

[73] The TMP cannot bind notice partners or notice-group partners.

[74] §6224(c)(3)(A). Likewise, ''[i]f a pass-thru partner enters into a settlement agreement with the Internal Revenue Service with respect to partnership items, that agreement binds all indirect partners holding an interest in that partnership through the pass-thru partner except those indirect partners who have been identified as provided in section 6223(c)(3) and §301.6223(c)-1 at least 30 days before the date on which the agreement is entered into.'' Reg. §301.6224(c)-2.

[75] Reg. §301.6231(a)(7)-1(b)(1).

[76] *Id.*

[77] Reg. §301.6231(a)(7)-2(a).

[78] Reg. §301.6231(a)(7)-2(b)(3).

[79] Reg. §301.6231(a)(7)-1(b)(2).

[80] Reg. §301.6231(a)(7)-1(c).

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partner with the largest profits interest is automatically the TMP, unless the IRS determines that this rule cannot be applied (e.g., no general partner has a profits interest).[81] If no partner is eligible to serve as the TMP under the regulations (including under the automatic designation rule), then the IRS may designate a partner to serve as the TMP,[82] as long as the partner was a partner in the partnership at the close of the taxable year under examination.[83] The IRS may designate a limited partner as the TMP if there is no general partner with a profits interest. Thus, partnerships cannot designate limited partners, non-managing members (when there are in fact managing members), or general partners without a profits interest in the partnership as the TMP.

While a partner may technically qualify to serve as TMP under the regulations, a number of other factors should inform the partners' selection of TMP. For example, partners may wish to avoid appointing a TMP with little or no economic stake in the partnership. For one, a TMP with limited financial stake may be less concerned about extending the statute of limitations, defending an IRS audit and challenges to the tax reporting of partnership items, filing suit, settlement terms, or filing a refund claim on behalf of the partnership. Partners should also be mindful of the potential duration of a TMP designation, which, unless revoked, remains in effect until the TMP's dies (or, in the case of an entity, liquidates), is incapacitated, resigns, or the TMP's partnership items become nonpartnership items.[84] Thus, the designation of a TMP for a taxable year may survive disposition of the TMP's partnership interest.

5. Protecting Partners' Rights

To protect their rights in TEFRA proceedings, partners should remember that Congress created the TMP to ease the burden on the IRS and allow the IRS to proceed against all partners in one unified proceeding, rather than in separate proceedings against each partner. At the same time, Congress intended to treat all partners in a partnership fairly and consistently. The TMP plays a central role in the tension between the goals of administrative efficiency, on the one hand, and consistent treatment of all partners, on the other. Specifically, the TMP's notice duties facilitate administrative economy, while theoretically protecting taxpayer rights and providing partners the choice between participating directly and allowing the TMP to participate on their behalf in the proceedings. In practice, however, TEFRA provides no right of action or remedy against the TMP (or the IRS) for any failure by the TMP to carry out its notice duties, and thus creates a potential trap for non-notice partners. For example, a non-notice partner who does not receive notice from the TMP may have no knowledge of the proceedings at all, and thus could be completely deprived of its ability to represent itself.[85] In that case, a private action against the TMP may not remedy the prejudice suffered in the TEFRA proceeding. In short, partners should be wary not to cede excessive control to the TMP, given partners' limited recourse against the TMP, and the minimal requirements placed on the IRS for protecting partner's rights.

Partners can, however, protect their rights by more fully delineating the TMP's duties and authority in the partnership agreement, to either expand or place limits on the TMP's powers. For example, the agreement could provide (1) that the partners have the right to review and consent to the filing of the partnership tax return or tax elections, such consent not to be unreasonably withheld; (2) that the TMP may not extend the partnership's statute of limitations without majority consent of the partners, by vote or value; (3) that the partners vote on any key decisions or actions during a partnership proceeding; and (4) more substantial notice requirements, with deadlines and remedies if the TMP fails to fulfill its duties. While partners should make sure to protect their rights, the partners should keep in mind that the partnership agreement ought to be sufficiently flexible so as to not prevent the TMP from effectively executing its duties. Additionally, the TMP may seek provisions in the agreement to ensure there are sufficient funds to cover the expenses that the partnership might incur from a TEFRA proceeding or to cover the TMP's expenses in carrying out its responsibilities. For example, the partnership agreement could specify how the partners will fund the hiring of outside counsel to assist during the administrative proceedings. Finally, while the IRS may not be bound to the parties' allocations of responsibility, the partnership agreement can at least create private, contractual remedies for breaches of duty.[86]

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[81] Reg. §301.6231(a)(7)-1(m)(2), §301.6231(a)(7)-1(n).

[82] Reg. §301.6231(a)(7)-1(p)(2). In so doing, the IRS must consider the criteria in Reg. §301.6231(a)(7)-1(q)(2).

[83] Reg. §301.6231(a)(7)-1(q)(1).

[84] Reg. §301.6231(a)(7)-1(l)(1).

[85] And, to the extent that the IRS follows the chief counsel advice discussed at n. 60 above and the accompanying text, notice partners would face the same problem.

[86] *See* CCA 201138026 (''Any arguable violation of the operating agreement by the TMP might at best create a cause of action by members of [the partnership] against each other, but would not limit the TMP's power under the TEFRA partnership provisions to represent the partners in the audit. *But see River City Ranches* (if IRS is aware that TMP is acting in violation of his fiduciary duty to other partners, IRS may not be able to rely on TMP).'').

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C. Adjustments Resulting from TEFRA Partnership Audits

1. Partnership Items (or Not)

The IRS can only adjust a ''partnership item'' of a TEFRA partnership in a partnership-level audit.[87] Conversely, the IRS cannot adjust partnership items in partner-level audits. Thus, the classification of an item as a partnership item (or not) is a threshold issue for determining whether TEFRA or regular deficiency procedures apply in order for the IRS to make adjustments to a partner's return, as well as for determining what remedies are available to a partner when the IRS makes such adjustments.

The statutory definition of ''partnership items'' is somewhat opaque, and merely provides that partnership items are those items ''required to be taken into account for the partnership's taxable year under any provision of subtitle A to the extent regulations prescribed by the Secretary provide that, for purposes of this subtitle, *such item is more appropriately determined at the partnership level* than at the partner level.''[88] The TEFRA regulations provide more clarity and specify that partnership items include, among other items: a partner's distributive share of the partnership's income, gain, loss, deduction, or credit; the amount, character, and changes in partnership liabilities; guaranteed payments; the partnership's statute of limitations; the determination of who is a partner of the partnership; and the accounting practices and legal and factual determinations that underlie the determination of partnership items.[89] Generally speaking, then, partnership items include all items reported on the partnership tax return, IRS Form 1065 and the Schedules K-1. A nonpartnership item is an item that is (or is treated as) not a partnership item. For example, unless there is a §754 election in effect, the purchase price paid by a partner when purchasing a partnership interest from another partner is a nonpartnership item. In that case, there is no need for the partnership to take the partner's purchase price into account for the partnership's taxable year.

Certain nonpartnership items are ''affected items,'' which are items that are affected by (but are not in and of themselves) partnership items.[90] Affected items generally are items that depend on the determinations of partnership items but do not universally apply to all partners. Stated another way, fact determinations specific or unique to a partner are necessary to make an adjustment to an affected item such that an adjustment could not be passed through to a partner based solely on the adjustment to the partnership item.[91] Examples of affected items include: (1) a partner's at-risk amount; (2) passive loss limitations; and (3) cancelation of indebtedness (''COD'') income.[92] Each of these items may be adjusted at the partnership level, but the impact to a particular partner cannot be known without making specific partner-level determinations. For example, assume that in a partnership proceeding, the IRS determines that a partnership is in receipt of $100 of COD income, which was not reported on the partnership return. Further assume that the IRS determines Partner A's distributive share of the COD income is $50. Before the IRS can determine the impact to Partner A' tax liability, the IRS must conduct a partner-level proceeding to determine issues such as whether or not Partner A is able to exclude the COD income from its taxable income, for example, under §108.

While the distinction between partnership and affected items may sound like a distinction without a difference, the distinction is meaningful indeed. The procedures available to the IRS to assess any resulting tax liability arising from a TEFRA partnership proceeding are determined by whether the adjusted item requires further partner-level determinations.

2. Assessing the Tax Liability Arising from TEFRA Audits: Flowing Through Adjustments to Partners' Returns: Computational Adjustments or Not?

Upon final determination of the tax treatment of any partnership items in a TEFRA proceeding (or by settlement), the IRS makes a computational adjustment to apply that determination to the tax liability of each partner.[93] A ''computational adjustment'' is the change in the tax liability of a partner that properly reflects the treatment of a partnership item.[94] The procedure for making a computational adjustment occurs either by direct assessment or through deficiency procedures initiated by an ''affected item'' notice of deficiency.[95]

The IRS may directly assess any tax liability attributable to partnership or certain affected items that do not require any partner-level factual determinations,

[87] §6221.

[88] §6231(a)(3) (emphasis added); Reg. §301.6231(a)(3)-1(a), §301.6231(a)(3)-1(b).

[89] Reg. §301.6231(a)(3)-1.

[90] §6231(a)(5).

[91] *See, e.g., Prochorenko v. United States*, 243 F.3d 1359, 1363 (Fed. Cir. 2001) (explaining that affected items are those that are dependent on a partner's own unique factual circumstances, and have no effect on and are not affected by the tax liability of any of the other partners); *Monti v. United States*, 223 F.3d 76, 82 (2d Cir. 2000).

[92] IRM 4.31.2.2.13 *et seq.* (June 20, 2013).

[93] §6230(a)(1).

[94] §6231(a)(6).

[95] §6230(a)(1), §6230(a)(2). *See United States v. Woods*, 134 S. Ct. 557, 563 (2013).

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i.e., "computational items."[96] Stated another way, these are changes in a partner's tax liability that can be mathematically calculated by substituting the partner's distributive share of the adjusted partnership items for the partner's distributive share of the originally reported partnership items on a partner's return. Direct assessment occurs by mailing the partner a notice of computational adjustment.[97] On the other hand, the IRS must follow normal deficiency procedures in order to assess affected items that require partner-level factual determinations, i.e., "substantive affected items."[98] In the latter case, the IRS cannot immediately assess the adjustments following the conclusion of the partnership proceeding, and the IRS must issue a notice of deficiency prior to assessment.[99]

The distinctions between partnership items, nonpartnership items, and affected items, and between computational items and substantive affected items, are important for a number of reasons.[100] First, the IRS cannot determine nonpartnership items in a partnership proceeding, and a partner cannot raise partner-level defenses in a partnership proceeding. However, when a partnership item is determined at the partnership level, while partner-level determinations may be required, a partner cannot wait until the partner-level proceeding to object to the partnership determination. Accordingly, the determination of the partnership item stands unless it is challenged in the partnership-level proceeding.[101] The Supreme Court recently explained the application of these principles in *Woods* as a two-stage structure, stating that with regard to the imposition of penalties arising from a partnership transaction, "TEFRA gives courts in partnership-level proceedings jurisdiction to determine the applicability of any penalty that could result from an adjustment to a partnership item, even if imposing the penalty would also require determining affected or non-partnership items such as outside basis. . . . Each partner remains free to raise, in subsequent partner-level proceedings, any reasons why the penalty may not be imposed specifically on him."[102] Put differently, the determination of the applicability of penalties that could result from an adjustment to a partnership item may itself be a partnership item, but partner-level defenses to penalty assessments must be made at the partner level.

Second, the period of limitations for challenging adjustments to partnership items depends on whether the adjusted item is a computational item, which is directly assessed via a notice of computational adjustment, or a substantive affected item, which is subject to normal deficiency proceedings. With regard to the former, taxpayers and practitioners may be surprised to learn that claims challenging most computational adjustments — i.e., those involving either (1) the erroneous computation of items on the partner's return consistent with the treatment on the partnership's return or to apply to the partner a settlement, an FPAA or the decision of a court, or (2) the erroneous imposition of any penalty or similar addition to tax which relates to an adjustment to a partnership item — must be brought within *six months* of receipt of the computational adjustment.[103]

Finally, the distinction between computational items and substantive affected items may determine the appropriate forum for litigation. As explained above, when the IRS assesses the tax attributable to substantive affected items, the IRS must issue the partner a notice of deficiency, which in turn allows the partner to challenge the assessment in Tax Court. Because the Tax Court is a prepayment forum, the partner can challenge the assessment without first paying the assessed tax. By contrast, if the IRS is able to directly assess the tax liability by issuing a notice of computational adjustment, then the IRS need not issue a notice of deficiency. If the taxpayer's timely objection to the computational adjustment is denied, the partner's only recourse to challenge the assessment is to pay the tax and sue for refund, in either a district court or the Court of Federal Claims.[104]

D. Varying Statutes of Limitations

1. Periods of Assessment

As explained above, with TEFRA, Congress established unified procedures for determining the tax treatment of partnership items at the partnership rather than the partner level.[105] One key objective of TEFRA is to treat all partners in the same partnership

[96] §6230(a)(1); Reg. §301.6231(a)(6)-1(a)(2); *Callaway v. Commissioner*, 231 F.3d 106, 110 n. 4 (2d Cir. 2000).

[97] Reg. §301.6231(a)(6)-1(a)(2).

[98] Reg. §301.6231(a)(6)-1(a)(1).

[99] *See* §6230(a)(2)(A)(i).

[100] There are myriad reasons that these distinctions are important; we have discussed a selected few of them here to provide a sense of the magnitude of the issues at stake.

[101] *See, e.g., Keener v. United States*, 551 F.3d 1358, 1364 (Fed. Cir. 2009) (explaining that when both partnership- and partner-level determinations must be made with regard to the imposition of tax-motivated interest under former §6621(c), if a partner fails to object to the partnership-level determinations during the partnership-level proceeding, then the partner has no right to challenge the partnership-level determinations in a partner-level proceeding).

[102] *United States v. Woods*, 134 S. Ct. 557, 564 (2013).

[103] §6230(c)(1)(A), §6230(c)(1)(C); §6230(c)(2)(A).

[104] §6226(e)(1). *See also* 28 U.S.C. §1346(a)(1); *Flora v. United States*, 362 U.S. 145 (1960).

[105] *See* I.B., above.

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consistently by resolving partnership items in a single proceeding. Consistent with this objective, Congress included a period of limitations for assessment of tax attributable to partnership items, §6229, within the TEFRA provisions. Nevertheless, the IRS and the courts have concluded that §6229 does not provide a single statute of limitations that applies to all partners. Rather, according to the IRS, the Tax Court,[106] the Fifth Circuit,[107] the Federal Circuit,[108] and the D.C. Circuit,[109] the period of limitations in §6229 merely provides for a minimum or extended period of assessment within which to assess the tax liability of all partners; it is the partner's specific period of limitations for making assessments under §6501 that controls.[110] Thus, courts have interpreted §6629 to create a minimum period during which assessments attributable to partnership items can be made, and this minimum period may expire before or after the maximum period provided in §6501. Hence, even though the period of limitations for assessment under §6229 may be closed, a TEFRA proceeding could still determine partnership items, and as long as a partner's §6501 period of limitations is open, the IRS can assess the tax liability for that partner. Accordingly, when partners have varying §6501 periods of limitations for assessment, these differing periods of assessment create the potential for disparate treatment of partners, and thereby undermine Congress's aim of consistent treatment of partners.

2. Period for Filing Administrative Refund Claims

To claim a credit or refund in a TEFRA proceeding, the TMP may file an administrative adjustment request (''AAR'') for the partnership, or any partner may file an AAR on its own behalf.[111] Perhaps counterintuitively, the time for filing an AAR is governed by the date the partnership return is filed, rather than when the partner's return is filed, or when the tax is paid.[112] Specifically, an AAR must be filed within three years of the later of (1) the date on which the partnership return is filed or (2) the last day for filing the partnership return, and before an FPAA is issued.[113] If the parties agree to extend the statute of limitations for assessing partnership items, the statute of limitations for filing an AAR is extended for the same period plus six months.[114] While any partner can file an AAR on its own behalf,[115] only the TMP can request substitute return treatment.[116] If the TMP requests substitute return treatment, then the IRS ''may treat the changes shown on such request as corrections of mathematical or clerical errors appearing on the partnership return.''[117] Partners thus should be mindful that TEFRA provides a mechanism, upon conclusion of an audit, for the TMP to effectively settle partnership items with the IRS for all partners by filing an AAR that reflects the IRS's adjustments and requesting substitute return treatment. This is yet another reason to carefully circumscribe the TMP's powers in the partnership agreement.

If the IRS denies the AAR or does not respond, a partner can file suit six months after filing the AAR, but no later than two years from filing the AAR.[118] If only the TMP files an AAR, then only the TMP can file suit.[119] If a partner files an AAR on its own behalf, and the TMP does not file an AAR or suit, then the partner can file a refund suit.[120] Because a partner must have filed its own AAR to seek judicial review if the TMP does not file suit, partners should consider filing their own AARs even if the TMP has already filed an AAR — particularly if their economic interests are not aligned.[121] By filing their own AARs, partners can avoid leaving their rights to judicial review in the hands of the TMP.

III. CONCLUSION

A partner's fate in a partnership audit depends in large part on a partner's understanding of the TEFRA rules. First, a partner cannot assume, simply because a partnership appears to qualify for the small partnership exception, that it in fact does. The presence of

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[106] *Rhone-Poulenc Surfactants & Specialties, LP v. Commissioner*, 114 T.C. 533, 551 (2000).

[107] *Curr-Spec Partners, LP v. Commissioner*, 579 F.3d 391, 401 (5th Cir. 2009).

[108] *A.D. Global Fund, LLC v. United States*, 481 F.3d 1351, 1355 (Fed. Cir. 2007).

[109] *Andantech LLC v. Commissioner*, 331 F.3d 972, 976–77 (D.C. Cir. 2003).

[110] While all circuit courts that have directly considered the relationship between §6229 and §6501 agree with the above interpretation, as least two circuit courts have suggested that §6229 provides for a single statute of limitations for partnership items. *See Desmet v. Commissioner*, 581 F.3d 297, 303 (6th Cir. 2009) (''If the petitioners are correct, then presumably the IRS will not be able to collect from them because the statute of limitations for direct assessment has run. *See* I.R.C. §6229.'' (citation omitted)); *Callaway v. Commissioner*, 231 F.3d 106, 110 (2d Cir. 2000).

[111] *See* IRM 4.31.4.1 (Sept. 1, 2006).

[112] §6227(a).

[113] *Id.*

[114] §6227(b).

[115] §6227(d).

[116] §6227(c)(1).

[117] §6227(c)(1)(B).

[118] §6228(b)(2)(B)(i).

[119] §6228(a)(1).

[120] §6228(b)(2)(A).

[121] While discussion of the TEFRA litigation procedures is beyond the scope of this article, we note that only notice partners can file suit.

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any pass-thru partner disqualifies a partnership from meeting the exception, and disregarded entities such as grantor trusts and SMLLCs are respected as pass-thru partners for this purpose. Should a taxpayer mistakenly believe that its partnership interest is not subject to TEFRA, it may lose its ability to make a claim to adjust its partnership items and the resulting tax liability at the partner level. Second, a partner must understand its ''partner classification'' and what that means in a TEFRA proceeding. Particularly, non-notice partners have few statutorily enforceable rights compared to notice partners. Thus, when warranted, partners should ensure notice and participation rights by following the identification rules to become a notice partner.[122] Otherwise, while every partner has a statutory right to participate in a TEFRA proceeding, a partner will not be able to meaningfully exercise that right without notice. As discussed, the IRS is required to provide NBAPs and FPAAs only to notice partners, and perhaps not even timely NBAPs, given recent chief counsel advice. Non-notice partners, therefore, are reliant on the TMP for information regarding a TEFRA proceeding and thus for their ability to exercise their participation rights.

At the other end of the spectrum, the TMP is afforded a number of exclusive rights, as well as responsibilities, that allow it to guide the partnership through the TEFRA proceeding. Because non-notice partners have no statutory remedy if the TMP breaches a duty, the partners should carefully identify the limits to the TMP's authority in the partnership agreement. Partners should consider whether to (1) expand the TMP's notice requirements and powers; (2) limit the TMP's ability to unilaterally extend the statute of limitations or bind partners in settlement by requiring that the majority of partners consent; and (3) require the TMP to defend IRS challenges and, if so, to what extent. Because the IRS may not be bound by allocations of power in the partnership agreement, partners should regularly review the TMP designation to ensure that it is appropriate for the partnership's current facts and circumstances.

TEFRA partners should also pay close attention to protect their rights to judicial review. Partners should be mindful that objections to certain computational adjustments must be made within six months. Further, objections to partnership-level determinations must be made during the partnership proceeding, and cannot be reserved for the follow-on partner-level proceeding, if any. The AAR procedures may also allow the TMP to effectively bind all partners to a settlement with the IRS.

By considering these issues, partners may be able to avoid unintended consequences of a lack of familiarity with the TEFRA procedures. If the history of partnership audits is any indication, there is no panacea for the difficulties partners face in partnership proceedings. Reform proposals may improve partnership proceedings, but, as TEFRA makes clear, legislative ''fixes'' inevitably beget problems of their own. In the meantime, partners should protect their rights and, to the greatest extent possible, prevent partnership problems from becoming partner-level problems.

[122] *See* §6223(c)(3).

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James Forsyth, Esq.

Buchanan Ingersoll & Rooney PC

One Oxford Centre

301 Grant Street, 20th Floor

Pittsburgh, PA 15219-14101700

Phone: (412) 562-3935

E-mail: james.forysth@bipc.com

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