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## **MTC Fall Meeting**

### **Adopting the MTC RAR/Partnership Audit Conformity Model: The Oregon Experience**

San Antonio, Texas

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## Overview

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- ▶ Changes to Partnership Audit Rules: The Centralized Federal Partnership Audit Regime & State Implications
- ▶ MTC Model Legislation
- ▶ Oregon Experience

- ▶ Changes to Partnership Audit Rules:  
The Centralized Partnership  
Audit Regime & State Implications

# Partnership Audit Rules Background

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- ▶ Bipartisan Budget Act of 2015 (HR 1314, P.L. 114-74)\* adopted new federal centralized audit regime for large partnerships
  - ▶ The new audit rules apply to tax periods after December 31, 2017
  - ▶ Projected \$9.3 Billion revenue-raiser
- ▶ Expected to raise additional tax revenue by enabling the IRS to more efficiently audit “large” partnerships and LLCs

\* Consolidated Appropriations Act of 2018, HR 1625 (P.L. 115-141), enacted in March 2018, made several technical corrections

# Centralized Partnership Audit Regime Overview

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- ▶ Centralized partnership audit regime (CPAR) applies to all Subchapter K entities.
- ▶ By default, audit adjustments assessed and collected at the entity level.
  - ▶ The partnership pays the tax, interest, and penalties on any “imputed underpayments” in the adjustment year.
  - ▶ The tax due is calculated at the highest corporate or individual rate (37% in 2018).
- ▶ Replaces “tax matters partner” with “partnership representative”
  - ▶ The partnership representative has the sole, exclusive authority to make decisions on behalf of the partnership which effect all the direct and indirect partners in IRS audit proceedings.

# Centralized Partnership Audit Regime Overview

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## ▶ Important Elections:

### ▶ Opt-Out Election: Section 6221 Election

- ▶ Applies only to “small” partnerships

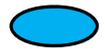
### ▶ Modification Period - 270-Day Period for Partners to Amend: Section 6225

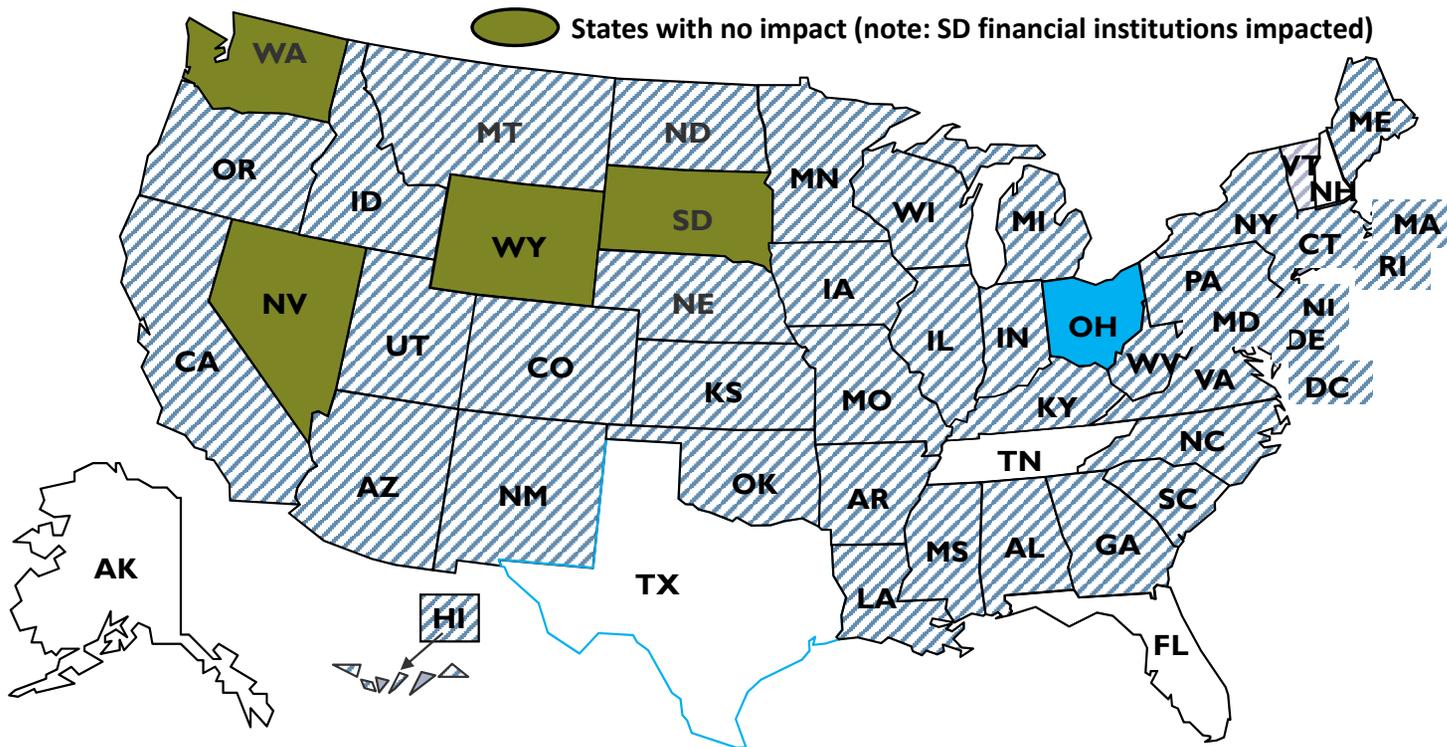
- ▶ One or more partners may file individual amended returns; or
- ▶ Partnership may demonstrate that a portion of the imputed underpayment is allocable to an entity with a lower tax rate than the highest marginal rate; or
- ▶ Partnership may make a “pull-in” election to have modifications made at the partner level.

### ▶ The Push-Out Election: Section 6226 Election

- ▶ The partnership may elect to have the partners report and pay the tax on current year returns.

# States Impacted by the Change

-  States imposing both a corp. income & personal income taxes
-  States only imposing a corp. tax or other impacted tax (note: NH imposes the BPT; TX imposes the Margin Tax; NH & TN tax interest and dividends for individuals)
-  States with impact limited to personal income tax
-  States with no impact (note: SD financial institutions impacted)



# State Impacts of New CPAR Rules

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- ▶ Issues the states need to address:
  - ▶ Does the states current law require a partnership subject to a CPAR audit to report the federal change?
    - ▶ Can partnerships simply file amended returns (entity returns along with any composite or withholding returns) and K-1s for partners and have partners file amended returns for the reviewed year?
  - ▶ Constitutional limitations
    - ▶ Nexus issues?
    - ▶ Proper allocation and apportionment of federal adjustments?

# MTC “Partnership Project” Work Group

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- ▶ Drafted amendments to the MTC model statute for reporting federal adjustments.
- ▶ The Interested Parties
  - ▶ ABA Section of Taxation SALT Committee Task Force (ABA)
  - ▶ American Institute of CPAs (AICPA)
  - ▶ Council On State Taxation (COST)
  - ▶ Institute for Professionals in Taxation (IPT)
  - ▶ Master Limited Partnership Association (MLPA)
  - ▶ Tax Executives Institute (TEI)

# ▶ MTC Model Legislation

# Model Uniform Statute for Reporting Adjustments to Federal Taxable Income and Federal Partnership Audit Adjustments

Section A—Definitions

**Section B—Reporting Adjustments to Federal Taxable Income – General Rule**

**Section C—Reporting Adjustments to Federal Taxable Income – Partnership Level Audit and Administrative Adjustment Request**

Section D—*De Minimis* Exception

Section E—Assessments of Additional [State] Tax, Interest, and Penalties Arising from Adjustments to Federal Taxable Income – Statute of Limitations

Section F—Estimated [State] Tax Payments During the Course of a Federal Audit

Section G—Claims for Refund or Credits of [State] Tax Arising from Federal Adjustments Made by the IRS

Section H—Scope of Adjustments and Extensions of Time

Section I—Effective Date

Optional Regulations

## How It's Accomplished: Reporting Federal Adjustments for Partnership Level Audits – Default Rule

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- ▶ Final determination date – all adjustments have been resolved
- ▶ Within 90 days of the final determination date, audited partnership must:
  - ▶ File a federal adjustments report;
  - ▶ Notify direct partners of their distributive share adjustments; and
  - ▶ File amended composite/withholding returns and pay the related tax liability on behalf of such partners as otherwise required by state law
- ▶ Within 180 days of the final determination date each direct partner
  - ▶ File a federal adjustment report with the state; and
  - ▶ Pay the additional tax, including penalty and interest, to the state (less any applicable credits)

## How It's Accomplished: Reporting Federal Adjustments for Partnership Level Audits – Election

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- ▶ Alternatively, within 90 days, the partnership can make an election to pay the tax for reviewed years.
  - ▶ File a federal adjustments report; and
  - ▶ Notify the state of the election
- ▶ Within 180 days of final determination date, the audited partnership shall:
  - ▶ Pay tax on behalf of partners based on calculation prescribed
  - ▶ Calculate tax at highest tax rate for each partner type
  - ▶ Treat indirect partners as resident partners (100% of adjustment taxable) unless the partnership can provide information showing residency of those partners—in which case apportionment rules apply
- ▶ Tiered partnerships are also eligible and must finalize all elections, reporting, and payment of the tax within 90 days after extended due date of the audited partnership's return for the adjustment year

## How It's Accomplished: Reporting Federal Adjustments for Partnership Level Audits – Election, cont.

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- ▶ Exceptions to the partnership pays election
  - ▶ Distributive share for unitary direct corporate partners excluded – adjustment must be reported by those corporate partners
  - ▶ Distributive share for tax exempt partners excluded
- ▶ Optional provisions to either allow or disallow partnership pays election where partnership did not have an initial filing obligation with a state in the reviewed year

# ▶ Oregon Experience

## Oregon Experience: Internal Process

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- ▶ MTC Member State
- ▶ Developed cross-agency team
- ▶ Analyzed and compared MTC model against Oregon statutes and rules
- ▶ Prepared legislative proposal
- ▶ Presented proposal to:
  - ▶ Agency Executive Management,
  - ▶ Department of Administrative Services, and
  - ▶ Governor's Office

## **Oregon Experience: Stakeholder Engagement**

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- ▶ Oregon Society of Certified Public Accountants
- ▶ Oregon State Bar, Tax Section
- ▶ Council On State Taxation
- ▶ American Institute of Certified Public Accountants
- ▶ Business lobby
  
- ▶ Oregon Legislative Counsel (drafters) for initial draft

## Oregon Experience: Legislative Engagement

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- ▶ Members of Revenue Committees and committee chairs
- ▶ Legislative Revenue Office
- ▶ Testified in House and Senate Committees
  - ▶ Joint testimony with COST
  - ▶ No business opposition
- ▶ Legislative Counsel to prepare amendments
- ▶ Prepared floor speeches for members to carry bill on floor of House and Senate

## **New Federal Partnership Audit Rules: State Implications**

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- ▶ State Legislative Activity to Date
  - ▶ 2016—only Arizona passed a bill
    - ▶ Arizona bill does not comprehensively address federal changes (e.g., fails to address tiered partnerships)
  - ▶ 2017—five states proposed legislation, but all died/failed
  - ▶ 2018—California, Georgia and Hawaii enacted conformity legislation
  - ▶ 2019—California (technical corrections), Ohio, Oregon, Rhode Island and West Virginia enacted conformity legislation

# ► Questions?

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