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IRS Provides Partnerships a Mechanism to Claim Benefit of Retroactive CARES Act Provisions

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Responding to requests for relief from the Real Estate Roundtable and others, the IRS issued Revenue Procedure 2020-23 on April 8, 2020 to address technical issues that would have limited the ability of partnerships and their partners to benefit from retroactive Coronavirus Aid, Relief, and Economic Security (CARES) Act provisions. The CARES Act contains various provisions that have retroactive effect. For example, under the CARES Act, "qualified improvement property"—improvements made to a building's interior after the building was first placed in service by owners of nonresidential real property, such as retail businesses and restaurants—qualifies for bonus depreciation and a 20-year useful life under the alternative depreciation system, retroactive to enactment of the Tax Cuts and Jobs Act (TCJA). Another retroactive CARES Act provision makes changes to the business interest expense deduction limitation rules under Section 163(j) enacted under the TCJA, and as a result, certain partnerships may want to reconsider associated elections made with previously filed tax returns. Taxpayers that could benefit from retroactive CARES Act changes generally would file amended tax returns to claim refunds of taxes paid with 2018 or 2019 tax returns. For partnership taxable years beginning after 2017, however, Section 6031(b) of the Internal Revenue Code does not permit partnerships to provide amended Schedules K-1 to partners after the due date for filing the partnership return, with exceptions for partnerships that have properly elected out of the partnership audit rules pursuant to Section 6221(b) of the Code (not available, for example, to a partnership with another partnership as a partner) or as otherwise provided by the Secretary of the Treasury. Revenue Procedure 2020-23 is an exercise of such authority.

Under the partnership audit rules applicable in taxable years beginning after 2017, a partnership wishing to make adjustments to a previously filed partnership return files an administrative adjustment request (AAR) pursuant to Section 6227 of the Code instead of an amended return. If the adjustment would be favorable for partners, the adjustment is pushed out to partners to affect partner tax returns only for the year in which the AAR is received (the "reporting year"). For example, under such rules, if a partnership could have deducted in the returns it filed for its taxable years ended December 31, 2018 and 2019 more depreciation for qualified improvement property under the CARES Act, partners would not be entitled to amend their 2018 and 2019 returns to claim their respective shares of the additional depreciation. Instead, the partners would take into account their respective shares of the additional depreciation as a tax adjustment only in the reporting year. If, for example, the reporting year was 2020 for the partnership's 2018 taxable year and the partner had losses in 2020, the partner would realize no benefit in 2020, with nothing to be carried to another year. The IRS recognized that the partnership audit rules inappropriately delay or deny the relief intended to be provided by the retroactive provisions in the CARES Act.

Revenue Procedure 2020-23 provides relief to partnerships that (1) have not elected out of the partnership audit rules; and (2) have filed, before issuance of Revenue Procedure 2020-23, a return on Form 1065 and furnished all required Schedules K-1 for a partnership taxable year beginning in 2018 or 2019 ("eligible partnerships"). An eligible partnership may (but is not required to) file an amended return for any such taxable year and furnish corresponding Schedules K-1 to partners before September 30, 2020. Such an amended return may make adjustments that are related or unrelated to CARES Act provisions. The amended return replaces the previously filed return and any AARs previously filed with respect to such return.

There are special rules for amended returns for taxable years under examination and taxable years with respect to which a partnership has previously filed an AAR and for partnerships that applied the proposed GILTI regulations under Section 951A.

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