

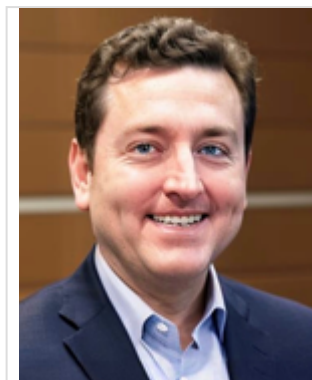
# Lessons from *SN Worthington*

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In this post, Armstrong continues his discussion of *SN Worthington*, saying the court's analysis in the case can be instructive as the IRS continues to emphasize partnership compliance.



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In a [prior post](#) I discussed how the Tax Court held that *SN Worthington's* election into the centralized partnership audit regime (CPAR) was valid in *SN Worthington Holdings LLC v. Commissioner*, [162 T.C. No. 10](#) (2024). The election into CPAR generally is only available with respect to a 2016 or 2017 partnership tax year. For tax years beginning in 2018, CPAR is the default audit regime unless an eligible partnership timely makes an election out. It is not readily apparent how many elections into CPAR the IRS has denied on similar grounds as *SN Worthington's*. Even if the specific issue decided by the court does not have far-reaching effects, however, the opinion still provides a helpful framework for analyzing the sufficiency of the elections in general and highlights certain procedural issues that could impact exams under the Bipartisan Budget Act of 2015 more generally. It's worth considering those issues in light of the IRS's enhanced focus on partnership compliance and as partnerships, practitioners, and the IRS wade deeper into the CPAR thicket.

## Determining the Validity of an Election

The opinion provides a helpful framework for analyzing the sufficiency of elections in other contexts. The opinion establishes the baseline principle that when Treasury and the IRS publish a rule and that rule imposes requirements to make an election, compliance with the plain text of those requirements ought to make the election valid. The government may not alter or expand upon those requirements at a later date when reviewing whether the taxpayer took all the proper steps to make the election. The government cannot create additional hoops for the taxpayer to jump through, beyond those requirements set forth in the rule governing the election.

Further, the government is presumed to mean what it says when writing the words that impose such requirements. Here, Treasury and the IRS could have drafted the regulation to require proof that the partnership's assets exceeded any potential underpayment; however, the language of the regulation states only that the election must include a *representation* that the partnership has sufficient assets to pay. The IRS tries to avoid the plain language of the rule, arguing that a "truthful" representation as contemplated by the regulation presupposes the partnership would be able to produce evidence of those sufficient assets. However, to the extent the IRS is arguing for the court to defer its own interpretation of reg. section 301.9100-22, *la Auer v. Robbins*, 519 U. S. 452 (1997), or *Kisor v. Wilkie*, [139 S. Ct. 2400](#) (2019), that is not apparent from the opinion. To the contrary, the Tax Court states: "When there is doubt to the meaning of a regulation, we interpret the regulation against the drafter."

## TEFRA Vs. BBA

In addition to its helpful analysis of what makes an election valid, the opinion teaches us that following the correct set of audit rules can be crucial to the propriety of the IRS's enforcement actions. Had the IRS respected SN Worthington's election into CPAR and proceeded to make its final adjustments through a BBA final notice, the outcome here likely would have been much different.

Following the correct procedures is not only critical to the validity of the enforcement action, however; the decision as to what procedures apply also controls who is going to act on behalf of the partnership during the proceeding, the scope of that proceeding, and ultimately who is liable for any tax resulting from the IRS's adjustments. Unlike the 1982 Tax Equity and Fiscal Responsibility Act, which permitted any notice partner to participate in the partnership exam, only the partnership representative can speak for and act on behalf of the partnership in a BBA audit. No other persons, outside of those authorized by a power of attorney, can take part in a proceeding governed by CPAR.

Whereas TEFRA was built on a dichotomy between partnership items (subject to determination at the partnership level) and affected items (subject to determination at the partner level), the scope of the BBA is intended to cover both types of items by allowing the IRS to adjust any "partnership-related item" in a BBA proceeding. The regulations broadly interpret the term "partnership-related item," reaching almost any item reported (or required to be reported) on a partnership return that has some effect (however remote) on chapter 1 income tax. Furthermore, as interpreted by the IRS the regulations can give rise to an imputed underpayment for the partnership even in cases in which the IRS is adjusting an informational item, or no tax would be due from the partners had all items been reported correctly. Each of these elements highlights the importance of identifying the correct procedure to audit and adjust the partnership return.

## Collecting an Unpaid Imputed Underpayment

The IRS argued before the Tax Court that a partnership cannot elect into CPAR unless it establishes it has sufficient assets to pay a potential BBA imputed underpayment. In addition to disagreeing with this read of reg. section 301.9100-22, the court found that the BBA procedures themselves refute the IRS's position. The court pointed specifically to section [6232\(f\)](#), which authorizes the IRS to assess and collect an unpaid imputed underpayment from the adjustment year partners of the partnership, or

from the former partners of a partnership that has ceased to exist. The implication is that if the IRS is concerned about a partnership with no assets electing into BBA, then it can turn to its authority under section [6232\(f\)](#) and collect the unpaid liability from the partnership's partners.

The only issue with that reasoning is that reg. section 301.9100-22 predated the enactment of section [6232\(f\)](#); the latter was added in March 2018 by the Tax Technical Corrections Act of 2018, whereas the former was proposed in August 2016. At the time the regulation was proposed, the only recourse under the statute to collect an unpaid imputed underpayment from the partners was through the cease-to-exist rules under section [6241\(7\)](#). That provision states a partnership adjustment must be taken into account by the former partners of a partnership that "ceases to exist".

The IRS's authority under the cease-to-exist provisions is limited. Unlike section [6232\(f\)](#), which permits a direct assessment against each partner, the cease-to-exist provisions do not authorize the IRS to collect the imputed underpayment itself from the partners. Rather, the cease-to-exist provisions require the partnership to push out the IRS adjustments underlying the imputed underpayment and rely on the partners to calculate and self-assess any tax due from the adjustments. Given the limited nature of its cease-to-exist tool, it is understandable why, at the time the regulations were proposed, the IRS tried to discourage collection-proof partnerships from electing into CPAR. (Granted, the IRS could have revisited and revised the rule after the Tax Technical Corrections Act was passed.)

## Why Didn't the IRS Use Dual Procedures?

What's hard to understand from the opinion is why the IRS did not follow both TEFRA and BBA procedures to guard against the result reached by the court. Had the IRS issued both a TEFRA final partnership administrative adjustment and a notice of final partnership adjustment under the BBA, the latter presumably would have given the court jurisdiction to hear the case (assuming SN Worthington timely filed a petition).

The IRS has an established history of using dual procedures when auditing partnerships and partners. Under TEFRA, for example, the IRS employed dual procedures when it was unclear whether an item was more appropriately determined at the partnership or partner level, and in situations where there was uncertainty as to whether an affected item required partner-level determinations. See, for example, [Chief Counsel Notice CC-2009-011](#) (March 11, 2009). Similar concerns seemingly would have animated the IRS's decisionmaking here where the dispute centered on what procedures should apply to the audit of SN Worthington's 2016 return.

The court's equitable estoppel analysis may offer some insight. Although SN Worthington believed it had made a valid election into BBA, the court found the partnership continued to communicate with the IRS and sign documents that referenced the TEFRA audit procedures. It was not until some point in 2020, after the section [6235](#) period to make BBA adjustments had expired, that SN Worthington raised an issue with the IRS's denial of the election. The Tax Court found these actions constituted misleading silence by SN Worthington. However, the court also found that the IRS was aware of all the facts needed to determine the election's validity. Had the IRS possessed enough information to

make a decision as to the election, presumably it also had sufficient data to consider whether to use dual procedures to hedge against the court disagreeing with that decision.