

## Legal Alert

### **NEW AUDIT RULES: PART 2 – THE PARTNERSHIP REPRESENTATIVE**

The Bipartisan Budget Act of 2015 (“BBA”) provides that partnerships and LLCs taxed as partnerships must appoint a Partnership Representative (“PR”). The PR need not be a partner or a member and will have substantially broader powers than the old Tax Matters Partner in connection with partnership audits.

The new audit rules provide that the PR has almost complete authority to act on behalf of the partnership or LLC (and therefore, effectively, the partners and members) when dealing with the IRS, without any requirement that the PR keep the partners, the members or the managers advised as to anything, even the very existence of the ongoing audit. The PR’s authority includes the ability to bind the partnership and the partners in the audit and other proceedings, including settlement authority and decisions on procedural issues such as whether to proceed to litigation. If a partnership or LLC does not designate a PR, the IRS will appoint one, and the LLC or partnership will have no say in who that designee might be.

Because of the significant authority granted to the PR, the partnership agreement or LLC operating agreement should address the PR’s status, authority and the limitations to be imposed on the exercise of this authority. The partnership agreement or LLC operating agreement can curtail those powers – for example, the PR could be required to notify the members or partners of not only the existence of an audit but of its progress and the communications to and from the IRS. Further, the partnership agreement or LLC operating agreement could require that some percentage of the partners must first agree to certain actions taken by the PR.

Provisions should also be included for how a PR is appointed and removed, and how a replacement PR is chosen. Since it is possible that a PR could have a conflict of interest in acting on behalf of the partnership, consideration must be given to imposing some level of duty on the PR to make an unbiased decision or at least provide for the replacement of the PR if it appears that there is a conflict of interest.

From the PR’s prospective, the LLC operating agreement or partnership agreement should require all partners to deliver all needed partnership level information, particularly that which would mitigate partnership level tax. The members should be required to file any amended tax returns as directed by the PR. Finally, the PR may well demand indemnification for any decisions undertaken in good faith.

As is clear from the foregoing, the provisions relating to the Tax Representative may well be extensive in any amended (and in any new) partnership or operating agreement.

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We've assembled a team of our business attorneys to help our clients evaluate the new audit rules and decide how to address them in their partnership agreement or LLC operating agreement. If you'd like to have us evaluate your situation, let us know at [New IRS Audit Rules@gblaw.com](mailto:New_IRS_Audit_Rules@gblaw.com). We look forward to hearing from you.

You can read the first alert of the series about who can opt out in [Part 1 of the New Audit Rules](#), and you can find more on our website about who pays the tax in [Part 3 of the New Audit Rules](#).