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Investors Brace for Partnership Tax Form Logistical Logjam (1)

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- Tax professionals weigh filing late or with estimates
- Amending returns costly, duplicates administrative burden

The expansion of tax reporting requirements for partnerships has created a problematic “logjam” with overlapping deadlines, delays in receiving information, and added work in talent-tight industries.

Investors receiving Schedule K-1s, for partners to disclose income, deductions and credit on [Form 1065](#), have a reporting dilemma: whether they should file on time with estimates and file an amended return later, or wait until after the deadline.

Two new schedules for Form 1065—[K-2 and K-3](#)—went into effect in 2021 to have taxpayers expand on the information relating to foreign income that is required in Schedule K-1. In January, the IRS updated the instructions to K-2 and K-3, but the forms drew [criticism](#) from practitioners.

“There is a fear that, given the talent shortage, and just the significant newness of any process around this, that this year there may be delays,” said Paul Phillips, FSO tax chief operational leader at EY, who works with insurance companies. “And providers may actually miss deadlines or may deliver partial results.”

Jeffrey Winkleman, a corporate taxation partner at Marcum LLP, said he has a client who is missing 100 K-1s when the company typically is missing approximately 15.

Any company that invests in a partnership, such as a corporation or a multi-tiered partnership, waits to receive a Schedule K-1. The deadline with extension for partnerships is Sept. 15—even

for multi-tiered partnerships that might be waiting on the form from another partnership due the same day. The deadline for corporations is Oct. 15.

“Everything’s compressed,” said Kristin Stone, a principal at Wolf and Company.

Industries such as hedge funds, asset management, and insurance will be most affected, waiting on flow-through investment information.

Investors and tax practitioners are faced with weighing the risks, costs, and time associated with deciding whether to file the returns on time without the Schedule K-1 or file late with the form.

“There is a belief that any efficiency that may have been gained through the K-3 information is now actually going to be wiped,” Phillips said.

He said tax departments and insurance companies will have to go through a “big reconciliation process” to determine whether or not their originally filed return was complete and accurate.

While Phillips said the timely receipt of information has been “greatly alleviated” over the past couple of years with new technology, some companies will create an internal deadline earlier than the official corporate filing date because the return process “has a lot of moving parts” and goes through tax preparation software. But it’s unclear what companies should do when the forms are received past the deadline.

Filing Decision

Having to file an amended return requires almost a duplication of administrative burden, tax pros said, and because it’s more time, it’s more costly for clients.

“Time is precious in this space,” Phillips said.

He said the expansion of the reporting requirements for partnerships has created a “logjam” for investors.

Winkleman said one choice “makes the most sense”: File on time, noting any estimates on Form 8082, and then file an amended return.

“It’s a more costly way of doing things, but in the long run, it’s the smarter way to do things,” Winkleman said. “It’s not what we’d like to do. We’d rather file it just once with everything in it.”

But you don't want to risk being late, because being late has penalties. There's some penalties associated with it." Winkleman added, "There's a lot at risk to filing a return late."

Elections on a tax return filed past the deadline could be ignored by the IRS because they have to be filed with a timely return, he said.

In multi-tiered partnerships, one partnership might be waiting for K-1s from another partnership before it can pass on its K-1 to another. Instead of filing an amended return, most partnerships are required to submit an [administrative adjustment request](#), which is more complicated and time consuming.

The administrative adjustment process is still new internally and for clients, tax pros said, adding they spend a lot of time in training and in educating the clients. The tax software is also not set up to handle the adjustment, Stone said.

Stone, who works with multi-tiered partnerships, said that as it gets closer to the deadline, she's going to look at which forms are missing K-3s and whether or not there are foreign taxes or international items, and try to find that answer from clients.

"There has to be something that makes us comfortable, that we're not missing something," Stone said. "But the problem is the IRS's approach was to get all this foreign information onto a unified form. So without seeing what's on it, there's just so much risk of not knowing what you're missing."

What's Needed

Tax pros expressed a range of needs from the IRS, with some asking for a deadline extension and others a new, simplified form.

Adam Sweet, a principal at Eide Bailly and former tax attorney at the IRS, said the agency should create a simplified process for certain amended returns. Currently, if even a name is changed on a K-1, it appears you have to file an amended return, he said.

"So some people have asked for some type of simplified procedures, like an EZ form," Sweet said.

Winkleman suggested extending the deadline. He said although the IRS might be reluctant to do that, getting the additional time to do the return right would be helpful.

The American Council of Life Insurers said in a statement that the group has been “regularly engaging” with the IRS on how to report late K-1s and asked for more guidance.

In [2021](#), the IRS allowed companies some penalty relief if they could prove a “good faith effort” to comply with the new reporting requirements.

“I think that the ask of the IRS to track things like interest, dividends, capital gains by country is something that takes a lot more time and effort,” Stone said. “And therefore I do think it’s going to delay K-1 issuances in the future. I don’t know that anyone will really be able to complete by April these days. They’re just making it more complicated.”