

**141.211 Audits performed and additional tax assessed at the partnership level.**

- (1) As used in this section:
- (a) "Administrative adjustment request" means an administrative adjustment request filed by a partnership under Section 6227 of the Internal Revenue Code;
  - (b) "Audited partnership" means a partnership subject to a partnership level audit resulting in a federal adjustment;
  - (c) "Corporate partner" means a partner that is subject to tax under KRS 141.040;
  - (d) "Direct partner" means a partner that holds an interest directly in a partnership or pass-through entity;
  - (e) "Exempt partner" means a partner that is exempt from taxation under KRS 141.040 (a) or (b);
  - (f)
    - 1. "Federal adjustment" means a change to an item or amount determined under the Internal Revenue Code that is used by a taxpayer to compute income tax owed to the Commonwealth, whether that change results from action by the:
      - a. Internal Revenue Service, including a partnership level audit; or
      - b. Filing of an amended federal return, federal refund claim, or an administrative adjustment request by the taxpayer.
    - 2. A federal adjustment is positive to the extent that it increases net income or taxable net income and is negative to the extent that it decreases net income or taxable net income;
  - (g) "Federal adjustments report" includes methods or forms required by the department for use by a taxpayer to report final federal adjustments, including an amended income tax return, information return, or a uniform multistate report;
  - (h) "Federal partnership representative" means the person:
    - 1. The partnership designates for the taxable year as the partnership's representative; or
    - 2. The Internal Revenue Service has appointed to act as the federal partnership representative, under Section 6223(a) of the Internal Revenue Code;
  - (i) "Final determination date" means the following:
    - 1. a. Except as provided in subparagraphs 2. and 3. of this paragraph, if the federal adjustment arises from any action by the Internal Revenue Service, the final determination date is the first day on which no federal adjustments arising from that action remain to be finally determined, whether by Internal Revenue Service decision with respect to which all rights of appeal have been waived or exhausted, by agreement, or, if appealed or contested, by a final decision with respect to which all rights of appeal have been waived or exhausted.

- b. For agreements required to be signed by the Internal Revenue Service and the taxpayer, the final determination date is the date upon which the last party signed the agreement;
  - 2. For federal adjustments arising from any action by the Internal Revenue Service, if the taxpayer filed as a member of a consolidated return under KRS 141.201 or a combined report under KRS 141.202, the final determination date means the first day on which no related federal adjustments arising from that action remain to be finally determined, as described in subparagraph 1. of this paragraph, for the entire group; and
  - 3. If the federal adjustment results from filing an amended federal return, a federal refund claim, or an administrative adjustment request, or if it is a federal adjustment reported on an amended federal return or other similar report filed under Section 6225(c) of the Internal Revenue Code, the final determination date means the day on which the amended return, refund claim, administrative adjustment request, or other similar report was filed;
- (j) "Final federal adjustment" means a federal adjustment after the final determination date for that federal adjustment has passed;
  - (k) "Indirect partner" means a partner in a partnership or pass-through entity and that partnership or pass-through entity holds an interest directly, or through another indirect partner, in a partnership or pass-through entity;
  - (l) "Nonresident partner" means an individual, trust, or estate partner that is not a resident partner;
  - (m) "Partner" means a person that holds an interest directly or indirectly in a partnership or other pass-through entity;
  - (n) "Partnership" means an entity subject to the provisions of Subchapter K of Chapter 1 of the Internal Revenue Code;
  - (o) "Partnership level audit" means an examination by the Internal Revenue Service at the partnership level under Subchapter C of Chapter 63 of the Internal Revenue Code, as enacted by Pub. L. No. 114-74, which results in a federal adjustment;
  - (p) "Pass-through entity" means an entity, other than a partnership, that is not subject to tax under KRS 141.040;
  - (q)
    - 1. "Reallocation adjustment" means a federal adjustment resulting from a partnership level audit or an administrative adjustment request that changes the shares of one (1) or more items of partnership income, gain, loss, expense, or credit allocated to direct partners.
    - 2. A positive reallocation adjustment means the portion of a reallocation adjustment that would increase federal income for one (1) or more direct partners.
    - 3. A negative reallocation adjustment means the portion of a reallocation adjustment that would decrease federal income for one (1) or more direct partners;

- (r) "Resident partner" means an individual, trust, or estate partner that is a resident for the relevant taxable year;
  - (s) "Reviewed year" means the taxable year of a partnership that is subject to a partnership level audit from which federal adjustments arise;
  - (t) "Taxpayer" has the same meaning as in KRS 131.010 and includes:
    - 1. a. A partnership subject to a partnership level audit; or
    - b. A partnership that has made an administrative adjustment request; and
    - 2. A tiered partner of the partnership described in subparagraph 1. of this paragraph; and
  - (u) "Tiered partner" means any partner that is a partnership or pass-through entity.
- (2) Except in the case of final federal adjustments that are required to be reported by a partnership and its partners under subsection (3) of this section, and final federal adjustments required to be reported for federal purposes under Section 6225(a)(2) of the Internal Revenue Code, a taxpayer shall report and pay any income tax due with respect to final federal adjustments arising from any action:
- (a) By the Internal Revenue Service; or
  - (b) Reported by the taxpayer on a timely filed amended federal income tax return, including a return or other similar report filed under Section 6225(c)(2) of the Internal Revenue Code, or federal claim for refund;
- by filing a federal adjustments report with the department for the reviewed year and, if applicable, paying the additional tax owed by the taxpayer no later than one hundred eighty (180) days after the final determination date.
- (3) (a) Except for adjustments required to be reported for federal purposes under Section 6225(a)(2) of the Internal Revenue Code, and the distributive share of adjustments that have been reported as required under subsection (2) of this section, partnerships and partners shall report final federal adjustments arising from a partnership level audit or an administrative adjustment request and make payments as under this subsection.
- (b) 1. With respect to an action required or allowed to be taken by a partnership under this subsection and a proceeding under KRS 131.110 with respect to that action, the state partnership representative for the reviewed year shall have the sole authority to act on behalf of the partnership, and the partnership's direct partners and indirect partners shall be bound by those actions.
  - 2. The state partnership representative for the reviewed year is the partnership's federal partnership representative unless the partnership designates in writing another person as its state partnership representative.
  - 3. The department may establish reasonable qualifications and procedures for designating a person, other than the federal partnership representative, to be the state partnership representative.

- (c) Final federal adjustments subject to the requirements of this subsection, except for those subject to a properly made election under subsection (4) of this section, shall be reported as follows:
  - 1. No later than ninety (90) days after the final determination date, the partnership shall:
    - a. File with the department a completed federal adjustments report, including all information required by the department;
    - b. Notify each of its direct partners of their distributive share of the final federal adjustments, including all information required by the department; and
    - c. File an amended composite return for direct partners or an amended withholding return for direct partners as required under KRS 141.206 and pay the additional amount of tax that would have been due had the final federal adjustments been reported properly as required; and
  - 2. No later than one hundred eighty (180) days after the final determination date, each direct partner that is taxed under KRS 141.020 or 141.040 shall:
    - a. File a federal adjustments report reporting their distributive share of the adjustments reported to them under subparagraph 1.b. of this paragraph; and
    - b. Pay any additional amount of tax due as if final federal adjustments had been properly reported, plus any penalty due under KRS 131.180 and interest due under KRS 131.183 and minus any credit for related amounts paid or withheld and remitted on behalf of the direct partner under subparagraph 1.c. of this paragraph.
- (4) An audited partnership making an election under this subsection shall:
  - (a) No later than ninety (90) days after the final determination date, file a completed federal adjustments report, including all information required by the department, and notify the department that it is making the election under this subsection; and
  - (b) No later than one hundred eighty (180) days after the final determination date, pay an amount, determined as follows, in lieu of taxes owed by its direct and indirect partners:
    - 1. Exclude from final federal adjustments the distributive share of these adjustments reported to a direct exempt partner not subject to tax under KRS 141.040(1)(a) or (b);
    - 2. For the total distributive shares of the remaining final federal adjustments reported to direct corporate partners subject to tax under KRS 141.040, apportion and allocate the adjustments under KRS 141.206 and multiply the resulting amount by the highest tax rate for the taxable year under KRS 141.040;

3. For the total distributive shares of the remaining final federal adjustments reported to nonresident direct partners subject to tax under KRS 141.020, determine the amount of the adjustments under KRS 141.206 based on what would be subject to tax as Kentucky-sourced income for a nonresident partner, and multiply the resulting amount by the highest tax rate for the taxable year under KRS 141.020;
  4. For the total distributive shares of the remaining final federal adjustments reported to tiered partners, determine the amount of the adjustments which is of a type that it would be subject to tax under KRS 141.206, less any amount that the audited partnership can determine to the department's satisfaction that is not subject to tax, and multiply that amount by the highest tax rate under KRS 141.020 or 141.040;
  5. For the total distributive shares of the remaining final federal adjustments reported to resident direct partners subject to tax under KRS 141.020, multiply that amount by the highest tax rate under KRS 141.020; and
  6. Add the amounts determined in subparagraphs 2. to 5. of this paragraph, and remit the amount along with penalty due under KRS 131.180 and interest due under KRS 131.183.
- (5) The election under subsection (4) of this section shall not apply to:
- (a) The distributive share of final audit adjustments that under KRS 141.202 that are included in the unitary business income of any direct or indirect corporate partner, provided that the audited partnership can reasonably determine this;
  - (b) Any final federal adjustments resulting from an administrative adjustment request; or
  - (c) Any audited partnership not otherwise subject to any reporting or payment obligation to this state.
- (6) (a) The direct and indirect partners of an audited partnership that are tiered partners and all of the partners of those tiered partners that are subject to tax under KRS 141.020 and 141.040 are subject to the reporting and payment requirements of subsection (3) of this section and the tiered partners are entitled to make the elections provided in subsection (4) of this section.
- (b) The tiered partners or their partners shall make the required reports and payments no later than ninety (90) days after the time for filing and furnishing statements to tiered partners and the partners under Section 6226 of the Internal Revenue Code and the regulations thereunder.
- (c) The department may promulgate administrative regulations to establish procedures and interim time periods for:
1. The reports and payments required by tiered partners and their partners;
  2. Making the elections under this section;
  3. The procedures related to the modified reporting and payment method under subsection (7) of this section; or

4. A de minimis amount upon which a taxpayer shall not be required to comply with this section.
- (7)
  - (a) Under procedures promulgated under KRS Chapter 13A by the department, an audited partnership or a tiered partner may enter into an agreement with the department to utilize an alternative reporting and payment method, including applicable time requirements for any other provision of this section, if the audited partnership or tiered partner demonstrates that the requested method will reasonably provide for the reporting and payment of taxes, penalties, and interest due under the provisions of this section.
  - (b) Application for approval of an alternative reporting and payment method shall be made by the audited partnership or tiered partner within the times established under subsection (4) or (6) of this section, as appropriate.
- (8)
  - (a) The election made under subsection (4) or (7) of this section is irrevocable, unless the department, in its discretion, determines otherwise.
  - (b) If properly reported and paid by the audited partnership or tiered partner, the amount determined under subsection (4) or (6) of this section shall be treated as paid in lieu of taxes owed by its direct and indirect partners, to the extent applicable, on the same final federal adjustments.
  - (c) The direct partners or indirect partners may not take any deduction or credit for this amount or claim a refund of the amount in this state.
  - (d) Nothing in this subsection shall preclude a direct resident partner from claiming a credit against taxes paid to this state under KRS Chapter 141, any amounts paid by the audited partnership or tiered partner on the resident partner's behalf to another state or local tax jurisdiction under KRS 141.070.
- (9) Nothing in this section prevents the department from assessing a direct partner or an indirect partner for taxes they owe, using the best information available, in the event that a partnership or tiered partner fails to timely make any report or payment required by this section for any reason.
- (10) The department shall assess additional tax, interest, and penalties resulting from any final federal adjustments arising from an audit by the Internal Revenue Service including a partnership level audit, reported by the taxpayer on an amended federal income tax return, or as part of an administrative adjustment request by the following dates:
  - (a) If a taxpayer files with the department a federal adjustments report or an amended Kentucky tax return as required within the periods under this section, the department may assess any amounts, including in-lieu-of amounts, taxes, interest, and penalties arising from those federal adjustments if the department issues a notice of the assessment to the taxpayer no later than the expiration of the one (1) year period following the date of filing with the department of the federal adjustments report; or
  - (b) If the taxpayer fails to file the federal adjustments report within the periods specified in subsection (2) or (3) of this section, as appropriate, or the federal adjustments report filed by the taxpayer omits final federal adjustments or

understates the correct amount of tax owed, the department may assess any amounts, including in-lieu-of amounts, taxes, interest, and penalties arising from the final federal adjustments, and absent fraud, if the department issues a notice of the assessment to the taxpayer no later than the expiration of the six (6) year period following the final determination date.

- (11) (a) A taxpayer may make estimated payments to the department, following the applicable process under KRS 141.207, of the tax expected to result from a pending Internal Revenue Service audit, prior to the due date of the federal adjustments report, without having to file the report with the department.
  - (b) The estimated tax payments shall be credited against any tax liability ultimately found to be due and will limit the accrual of further statutory interest on that amount.
  - (c) If the estimated tax payments exceed the final tax liability and statutory interest ultimately determined to be due, the taxpayer is entitled to a refund or credit for the excess, provided the taxpayer filed a federal adjustments report or claim for refund or credit of tax under this section no later than one (1) year following the final determination date.
- (12) (a) Except for final federal adjustments required to be reported for federal purposes under Section 6225(a)(2) of this Internal Revenue Code, a taxpayer may file a claim for refund or credit of tax arising from federal adjustments made by the Internal Revenue Service on or before the later of:
- 1. The expiration of the last day for filing a claim for refund or credit under KRS 134.580; or
  - 2. One (1) year from the date a federal adjustments report under subsection (2) or (3) of this section, as applicable, was due to the department.
- (b) The federal adjustments report shall serve as the means for the taxpayer to report additional tax due, report a claim for refund or credit of tax, and make other adjustments, including any net operating loss, resulting from adjustments to the taxpayer's federal taxable income.
- (13) (a) Unless otherwise agreed in writing by the taxpayer and the department, any adjustments by the department or by the taxpayer made after the expiration of the time allowed under KRS 141.210 is limited to changes to the taxpayer's tax liability arising from federal adjustments.
- (b) The time periods provided for in this section may be extended, upon written agreement between the taxpayer and the department, based on the complexity of the federal adjustment or the number of direct partners or tiered partners.
  - (c) The time period shall be automatically extended, upon written notice to the department, by sixty (60) days for an audited partnership or tiered partner which has ten thousand (10,000) or more direct partners.
  - (d) Any extension granted under this subsection for filing the federal adjustments report extends the last day prescribed by law for assessing any additional tax arising from the adjustments to federal taxable income and the period for filing a claim for refund or credit of taxes.

**Effective:** April 15, 2020

**History:** Created 2020 Ky. Acts ch. 91, sec. 57, effective April 15, 2020.