

Release of draft 2019 Form 1065 and its Schedule K-1

On September 30, 2019, the IRS released a draft of the tax year 2019 [Form 1065, U.S. Return of Partnership Income](#) and its [Schedule K-1, Partner's Share of Income, Deductions, Credits, etc.](#) The changes are intended to assist the IRS in assessing compliance risk and identifying potential noncompliance. Similar changes were made to the draft 2019 tax forms for S corporations (i.e., the [Form 1120-S U.S. Income Tax Return for an S Corporation](#) and its [Schedule K-1 \(Form 1120-S\)](#)). The IRS has not yet released accompanying instructions but describe the draft forms as “near-final.” Comments are due within 30 days of the release with the expectation that the forms may be finalized by December 2019. The accompanying instructions have not yet been released.

Assuming the draft form is finalized without change, significant additional time may be required to comply with the new form for the 2019 filing season. Among the more significant changes to the Schedule K-1 (Form 1065) is the requirement that a partnership report each partner's tax basis capital account rollforward. For the tax year 2018, by contrast, a tax basis capital account disclosure was required **only** if a partner had a negative tax basis capital account at the beginning of the year or at the end of the year, and only the beginning and ending negative tax capital accounts were required to be disclosed.

In addition, the updated Schedule K-1 (Form 1065) requires that a partnership report each partner's share of:

- Net unrecognized section 704(c) gain or loss, relating to contributions or revaluations of appreciated or depreciated property, determined both at the beginning and at the end of the applicable taxable year
- Income or other items related to section 743(b) negative adjustments
- Guaranteed payments for services
- Guaranteed payments for capital
- Section 751 “hot” asset gain or loss
- Certain other items.

Notably, although on its face the updated Schedule K-1 (Form 1065) appears limited to disclosure of a partner's “net unrecognized section 704(c) gain or loss,” the updated Schedule K-1 (Form 1065) also requires that a partnership disclose to its partners certain additional, but currently unspecified, section 704(c) information. Thus, it is possible that the IRS could require additional information to be reported.

The draft 2019 Form 1065 and Schedule K-1 (Form 1065) also require information that could provide certain audit or statistical data points, including:

- The number of foreign partners subject U.S. federal income tax pursuant to section 864(c)(8) as a result of a transfer of all or a portion of a partnership interest or receipt of a partnership distribution
- Whether any transfers between the partnership and its partners were subject to the disguised sale disclosure requirements under Treas. Reg. section 1.707-8
- Whether the partnership aggregated or grouped activities for section 465 at risk and section 496 passive activity purposes
- Whether the partnership has more than one activity for section 465 at risk and section 469 passive activity purposes
- Whether a decrease in a partner's share of partnership profit, loss, or capital is due to a sale or exchange of partnership interest
- Whether partnership liabilities include liabilities of a lower-tier partnership.

Lastly, it is worth noting that, to date, the draft Form 1065 has not been revised to provide specific reporting within the capital gains boxes of long-term capital gains that have a holding period of three years or less for purposes of the “carried interest” rules of section 1061.

The numerous proposed changes to the updated Form 1065 and Schedule K-1 (Form 1065) likely will add significant additional time to the tax reporting compliance process. Partnerships should assess the new changes and discuss with their tax advisor what additional effort may be required to comply with the required reporting. Therefore, it will be important to assess tax reporting and compliance readiness well in anticipation of filing deadlines.

Contact your KPMG engagement team for further information regarding the updated Form 1065 and Schedule K-1 (Form 1065).

Contact information

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