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From:
Sent: Wednesday, May 28, 2025 03:32:03 PM
To:
Cc:
Bcc:
Subject: RE: Inquiry to Counsel Regarding Late Filed AARs with ERC Issue

Hi [redacted]:

I hope this message finds you well. I'm writing to share P&A 6/7's advice on the first three questions—

(1) Whether the Service can process AARs and assess IUs shown on them when the AARs were filed after the 3-year deadline under IRC 6227(c);
(2) Whether the Service can process AARs and assess IUs shown on them when the AARs lack a proper PR signature;
(3) If the answer to (1) or (2) is no, what are the alternative procedures taxpayers should follow when they fail to file a timely and/or valid AAR to report the income tax changes required due to the ERC received.

The fourth question was how the Service should handle payments associated with the IUs reported (i.e., whether the payments should be refunded to the taxpayer pending the completion of the alternative actions described for question (3)). We've realized that question should be addressed with P&A Branches 3 and 4, who handle refunds, offset, and related issues, and have reached out to them for their advice on it. I'll be sure to share their advice on that aspect of the question as soon as we have it.

The answers to the three questions described above are explained in the attached memorandum and summarized below. Please let me know if you have follow-up questions or would like to discuss. I will be OOO during the week of June 9-13, but I can schedule a call for later this week or next week if that would be helpful.

Question 1

Section 6227(c) uses mandatory language to describe the date by which a partnership must file an AAR, and the Regulations also do not appear to give the Service any discretion to accept or process an AAR filed after the section 6227(c) date (or to assess an IU shown on the AAR).

Question 2

Similarly, while the Regulations give the Service to accept AARs even if certain other information is missing, neither the Code nor the Regulations give the Service any discretion to accept an AAR that lacks a valid PR/DI signature. As a result, AARs that lack a valid PR/DI signature cannot be accepted or processed, and IUs shown on those AARs cannot be assessed.

Question 3

The memorandum contains more detailed instructions for how taxpayers should file an AAR to report income tax changes from receiving the ERC for the tax year during which they received the ERC if section 6227(c) prevents them from filing an AAR for the tax year for which they received the ERC. The steps that taxpayers should take depend on whether the section 6227(c) date has passed for the tax year during which they received the ERC, and whether the taxpayers have already filed a partnership return for that tax year.

Please let me know if you have any questions or concerns or would like to discuss. My apologies for the delay in getting you this advice, and the advice on the payment issue.

Thank you very much,

[redacted]

Questions presented

(1) Can the Service process administrative adjustment requests (AARs) submitted to correct wage expense deductions and assess imputed underpayments (IUs) stated on those AARs after section 6227(c)'s deadline has passed?
(2) Can the Service process AARs submitted for the same purpose that lack required signatures (i.e., the partnership representative or designated individual's signature) or a valid designation or appointment of a partnership representative or designated individual?
(3) If the answer to either (1) or (2) is no, what are the alternative procedures that taxpayers should follow to correct their failure to reduce their wage expense deduction?

Background

If a taxpayer receives an ERC for a tax year, the taxpayer must reduce its wage expense deduction for the same tax year by a corresponding amount. 26 U.S.C. § 3134(e). However, some taxpayers claimed the ERC without first reducing their wage expense deductions. Some partnerships subsequently attempted to reduce their wage expense deductions by submitting AARs that were untimely, lacked required signatures, or lacked a valid designation/appointment of a partnership representative or designated individual.

1. Statutes of limitations for filing AARs and making partnership adjustments.

A partnership may file an AAR to request an adjustment to one or more partnership-related items (PRIs) for a tax year. However, the partnership cannot file an AAR for a tax year more than three years after the later of: (1) the date on which the partnership return for the tax year was filed, or (2) the partnership return due date for the tax year (determined without regard to extensions). *Id.* § 6227(c); *see also* Treas. Reg. § 301.6227-1(b); IRM 4.31.9.7.7.1(5) (01-24-2024). Additionally, the partnership cannot file an AAR after the Service has mailed a notice of administrative proceeding (NAP) to the partnership. 26 U.S.C. § 6227(c).

2. Signature requirements for AARs.

In the BBA context, the "partnership representative" has "the sole authority to act on behalf of the partnership under [the BBA] subchapter." 26 U.S.C. § 6223(a); Treas. Reg. § 301.6223-2(d)(1). As a result, only the partnership representative can file an AAR under section 6227. *See* Treas. Reg. § 301.6227-1(c)(1) ("An AAR… must be signed under penalties of perjury by the partnership representative"); IRM 4.31.9.9.7.7.1(3) (01-24-2024) ("Only the PR (or DI, if applicable) may sign and file an AAR on behalf of the partnership.").

The BBA regulations also indicate the Service does not have discretion to accept or process AARs that are not signed by a validly designated/appointed partnership representative or designated individual. Namely, the regulations require an AAR to include certain other information but state that, if some or all the information is missing, the Service "may, but is not required to, invalidate [the] AAR or readjust any items that were adjusted on the AAR." Treas. Reg. § 301.6227-1(c)(2). In contrast, the regulations do not give the Service discretion over whether to accept an AAR that has not been signed under penalties of perjury by the partnership representative or designated individual. *See id.* § 301.6227-1(c)(1). As a result, the Service cannot accept an AAR that lacks a required signature or a valid designation or appointment.

3. The "Frequently asked questions about the Employee Retention Credit" webpage.

On the Service's ERC FAQs webpage, Question 2 in the "Income tax and ERC" section asks, "I claimed the ERC but didn't reduce my wage expenses on my income tax return. The ERC claim was paid in a subsequent year. What do I do?" The answer states—

> Under these facts, you're not required to file an amended return or, if applicable, an administrative adjustment request (AAR) to address the overstated wage expenses. Instead, you can include the overstated wage expense amount as gross income on your income tax return for the tax year when you received the ERC.

The answer also explains that this approach is based on the tax benefit rule, which requires a taxpayer to "include a previously deducted amount in income when a later event occurs that is fundamentally inconsistent with the premise on which the deduction is based." Here, the receipt of the ERC is fundamentally inconsistent with the uncorrected wage expense deduction.

Application

1. The Service cannot accept or process AARs filed after the expiration of the section 6227(c) period.

A partnership cannot file an AAR for a tax year more than three years after the later of: (1) the date on which the partnership return for the tax year was filed, or (2) the partnership return due date for the tax year (determined without regard to extensions). 26 U.S.C. § 6227(c). The Code describes this time limit in mandatory terms: "A partnership **may not file** such a request after…," *id.* (emphasis added), and the BBA regulations do not provide a basis for the Service to accept an AAR after the date described in section 6227(c). *See* Treas. Reg. § 301.6227-1(b).

As a result, the Service cannot accept AARs filed by partnerships after the end of the section 6227(c) period.

2. The Service cannot accept or process AARs that have not been signed by a validly designated partnership representative.

The partnership representative (or designated individual, if applicable) must sign the AAR. Treas. Reg. § 301.6227-1(c)(1); *see also* IRM 4.31.9.9.7.7.1(3) (01-24-2024). As such, the Service cannot accept or process an AAR that was not signed by a validly designated partnership representative (or designated individual, if applicable). Additionally, the submission of an invalid AAR does not toll or otherwise extend the section 6227(c) period. Thus, the fact that a partnership submitted an invalid AAR before the end of the section 6227(c) period does not permit the Service to accept a valid AAR filed by the partnership after the end of the section 6227(c) period.

3. If a partnership is barred from adjusting its wage expense deduction for the year for which it claimed the ERC by section 6227(c) or 6235, the partnership should include the amount by which its wage expense deduction was overstated in its income for the tax year during which it received the ERC.

The Service's ERC FAQs state that if a taxpayer claimed the ERC but did not reduce its wage expense deduction, the taxpayer is not required to file an amended return or AAR

to adjust the deduction, but instead "can include the overstated wage expense amount as gross income on your income tax return for the tax year when you received the ERC." The steps that partnerships should take to comply with this direction depend on when the partnership received the ERC; that is, the answer depends on the tax year in which the Service refunded or credited the ERC to the partnership, not the tax year in which the partnership paid the qualified wages.

a. The partnership has not yet received the ERC or received the ERC in a tax year for which it has not yet filed its partnership return.

If a partnership has not yet received the ERC, then the partnership should report the ERC as income for the tax year in which the Service credits or refunds the ERC to it. For example, if the Service pays a refundable ERC to a partnership during tax year 2025, the partnership should include the amount of the ERC as income on its 2025 partnership return. Additionally, if the Service credited or refunded an ERC to a partnership during tax year 2024 and the partnership has not yet filed its 2024 partnership return (because, for example, it received a six-month extension to file), the partnership should include the amount of the ERC as income on its 2024 partnership return when it files the return.

b. The partnership received the ERC in a tax year for which it has filed its partnership return, and the partnership has not yet filed an AAR for that tax year.

If the Service credited or refunded an ERC to a partnership during a prior tax year (e.g., 2022, 2023, 2024) and the partnership already filed its partnership return for the tax year, then the partnership should file an AAR for that tax year to adjust its income based on the inclusion of the amount of the ERC. For example, if: (1) a partnership claimed an ERC based on qualified wages paid during tax year 2020, (2) the partnership failed to reduce its 2020 wage expense deduction by the amount of the ERC, (3) the Service paid the ERC to the partnership during tax year 2023, and (4) the partnership has already filed its 2023 partnership return, then the partnership should file an AAR for tax year 2023 to increase its income by the amount of the ERC.

The inclusion of the ERC in the partnership's income will be a "positive adjustment," Treas. Reg. § 301.6225-1(d)(2)(iii), and will result in the partnership owing an IU. When the partnership files the AAR, it must either pay the IU reflected on the AAR or elect to have the reviewed year partners take their pro rata shares of the positive adjustment to income into account. *Id.* §§ 301.6227-2(b)(1), (c).

c. The partnership received the ERC during a tax year for which it has filed its partnership return, but the section 6227(c) period for filing an AAR for that tax year has closed.

If the Service credited or refunded an ERC to a partnership during a prior tax year, the partnership already filed its partnership return for the tax year, and the section 6227(c) period for filing an AAR for that tax year has closed, then the partnership does not have a way to include the ERC in its income. Consider a scenario in which the Service paid an ERC to a partnership during tax year 2021. If the partnership filed its partnership

return on April 15, 2022, then under section 6227(c), the last date when the partnership can file an AAR for tax year 2021 is April 15, 2025. If the partnership does not file an AAR by April 15, 2025, then the partnership will be unable to include the amount of the ERC in its income for the tax year when the Service credited or refunded the ERC to it. Currently, this scenario would only arise with respect to partnerships that received the ERC (as a credit, refund, or offset) during tax year 2021.