SN Worthington Holdings LLC v. Commissioner of Internal Revenue, 162 T. C. No. 10 (2024)

In a landmark decision, the U. S. Tax Court ruled that SN Worthington Holdings LLC's election into the Bipartisan Budget Act (BBA) audit procedures was valid despite the IRS's objections. The court held that when a partnership complies with all regulatory requirements for an election, it is valid, and the IRS must follow the elected procedures. This ruling invalidates the IRS's use of TEFRA procedures and the subsequent Final Partnership Administrative Adjustment (FPAA) issued under those procedures, marking a significant clarification on the application of BBA election rules.

Parties

SN Worthington Holdings LLC, formerly known as Jacobs West St. Clair Acquisition LLC, with MM Worthington Inc. as the Tax Matters Partner (TMP), was the petitioner. The Commissioner of Internal Revenue was the respondent.

Facts

SN Worthington Holdings LLC, an Ohio limited liability company classified as a partnership for federal income tax purposes, filed a partnership return for the 2016 tax year. In 2018, upon notification from the Commissioner of an examination of its return, SN Worthington elected to be subject to the partnership audit and litigation procedures under the Bipartisan Budget Act of 2015 (BBA). The election required SN Worthington to represent that it had sufficient assets to pay any potential imputed underpayment. The Commissioner rejected this election, asserting that SN Worthington lacked the necessary assets. Despite the rejection, SN Worthington continued communications with the Commissioner, signing documents referencing TEFRA procedures. In 2020, SN Worthington contested the use of TEFRA procedures, arguing that its BBA election was valid.

Procedural History

The Commissioner initiated an examination of SN Worthington's 2016 return and notified SN Worthington of its option to elect into the BBA procedures. SN Worthington made the election within the required timeframe using Form 7036. The Commissioner rejected the election, citing insufficient assets, and proceeded with the examination under TEFRA procedures. On August 24, 2020, the Commissioner issued a Notice of Final Partnership Administrative Adjustment (FPAA) under TEFRA. SN Worthington challenged the FPAA's validity, arguing that the BBA election was valid and that the FPAA was therefore invalid. The Tax Court heard the case, with the Commissioner arguing that the election was invalid and that SN Worthington should be equitably estopped from asserting the BBA election's validity.

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Issue(s)

Whether SN Worthington Holdings LLC made a valid election into the BBA partnership audit and litigation procedures for its 2016 tax year, thereby rendering the Commissioner's issuance of a Final Partnership Administrative Adjustment (FPAA) under TEFRA invalid?

Rule(s) of Law

To elect into the BBA procedures for years before 2018, a partnership must submit an election under Treasury Regulation § 301. 9100-22(b)(2) that satisfies the requirements set forth in that regulation. One of the requirements is a representation that "[t]he partnership has sufficient assets, and reasonably anticipates having sufficient assets, to pay a potential imputed underpayment with respect to the partnership taxable year. " (Treas. Reg. § 301. 9100-22(b)(2)(ii)(E)(4)).

Holding

The Tax Court held that SN Worthington's election into the BBA procedures was valid because it complied with all requirements under Treasury Regulation § 301. 9100-22(b)(2). Consequently, the FPAA issued under the repealed TEFRA procedures was invalid, and the court lacked jurisdiction over the TEFRA partnership case.

Reasoning

The court reasoned that SN Worthington's compliance with the plain text of the regulatory election requirements was sufficient to validate the election. The court emphasized that the Commissioner cannot impose additional requirements beyond those stated in the regulation. The court rejected the Commissioner's argument that SN Worthington needed to prove its asset sufficiency beyond the representation required by the regulation, citing that the BBA procedures themselves account for partnerships with insufficient assets by allowing the Commissioner to assess and collect from partners. The court also addressed the Commissioner's equitable estoppel argument, concluding that it did not apply because the Commissioner had all relevant facts to determine the election's validity and incorrectly applied the law to those facts. The court's decision underscores the importance of adhering to regulatory text in the context of BBA elections and clarifies the procedural framework for partnerships transitioning to the new audit regime.

Disposition

The Tax Court dismissed the case for lack of jurisdiction, as the FPAA issued under TEFRA was invalid due to SN Worthington's valid BBA election.

Significance/Impact

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This decision significantly impacts the application of the BBA audit procedures, affirming that partnerships can validly elect into these procedures by complying with regulatory requirements without additional burdens imposed by the IRS. It clarifies the boundaries of IRS authority in challenging such elections and underscores the importance of the regulatory text in determining the validity of elections. The ruling may influence future cases involving BBA elections and could lead to a reevaluation of IRS procedures for handling such elections. It also reinforces the transition from TEFRA to BBA procedures, ensuring that partnerships that have elected into the BBA regime are subject to the correct audit and litigation processes.

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