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Revenue Procedure 84-35

January 1984

SECTION 1. PURPOSE

The purpose of this revenue procedure is to update *Rev. Proc. 81-11, 1981-1 C.B. 651*, to conform to the small partnership provisions of *section 6231 (a) (1) (B) of the Internal Revenue Code*. *Rev. Proc. 81-11* sets forth the procedures under which partnerships with 10 or fewer partners will not be subject to the penalty imposed by *section 6698* for failure to file a partnership return.

SEC. 2. BACKGROUND

.01 *Section 6031 (a) of the Code* provides that every partnership must make a return for each taxable year including all information that the Secretary may by forms and regulations prescribe.

.02 *Section 402 of the Tax Equity and Fiscal Responsibility Act of 1982, 1982-2 C.B. 462, 585*, added *sections 6221 through 6232* to the Code to provide that the tax treatment of partnership items must be determined at the partnership level. For purposes of these sections, *section 6231 (a) (1) (A)* defines "partnership" to mean any partnership required to file a return under *section 6031 (a)* except as provided in *section 6231 (a) (1) (B)*.

.03 *Section 6231 (a) (1) (B) of the Code* provides an exception to the definition of "partnership" for small partnerships. In general, the term "partnership" does not include a partnership if the partnership has 10 or fewer partners, each of whom is a natural person (other than a nonresident alien) or an estate, and each partner's share of each partnership item is the same as such partner's share of every other item. A husband and wife, and their estates, are treated as one partner for this purpose.

.04 *Section 6698 of the Code* imposes a penalty if any partnership required to file a return under *section 6031* fails to file a timely return, or files a return that fails to show the information required by that section, unless the failure is due to reasonable cause.

.05 The Conference Committee Report concerning *section 6698 of the Code* states:

The penalty will not be imposed if the partnership can show reasonable cause for failure to file a complete or timely return. Smaller partnerships (those with 10 or fewer partners) will not be subject to the penalty under this reasonable cause test so long as each partner fully reports his share of the income, deductions, and credits of the partnership...

H.R. Rep No. 95-1800 (Conf. Report), 95th Cong., 2d Sess. 221 (1978), 1978-3 C.B. (Vol. 1) 521, 555. See also H.R. Rep. No. 95-1445, 95th Cong., 2d Sess. 75 (1978), 1978-3 C.B. (Vol. 1) 181, 249, and S. Rep. No. 95-1263, 95th Cong., 2d Sess. 106 (1978), 1978-3 C.B. (Vol. 1) 315, 403, which contain similar statements.

SEC. 3. REQUIRED PROCEDURES

.01 A domestic partnership composed of 10 or fewer partners and coming within the exceptions outlined in *section 6231 (a) (1) (B) of the Code* will be considered to have met the reasonable cause test and will not be subject to the penalty imposed by *section 6698* for the failure to file a complete or timely partnership return, provided that the partnership, or any of the partners, establishes, if so requested by the Internal Revenue Service, that all partners have fully reported their shares of the income, deductions, and credits of the partnership on their timely filed income tax returns.

.02 Partnerships having a trust or corporation as a partner, tier partnerships, and partnerships where each partner's interest in the capital and profits are not owned in the same proportion, or where all items of income, deductions, and credits are not allocated in proportion to the prorata interests, do not come within the exception provisions of *section 6231 (a) (1) (B) of the Code* and, are subject to the penalty imposed by *section 6698*.

.03 Although a partnership of 10 or fewer partners may not be automatically excepted from the penalty imposed by *section 6698 of the Code* under section 3.01, the partnership may show other reasonable cause for failure to file a complete or timely partnership return.

.04 In determining whether a partner has fully reported the partner's share of the income, deductions, and credits of the partnership, for purposes of section 3.01, all the relevant facts and circumstances will be taken into account. In making this determination, the nature and materiality of any error or omission will be considered. For example, although an isolated clerical error normally reflects no more than mere inadvertence, such an error may be of such magnitude that the partner will not be considered to have fully reported. If the error or omission results in a de minimis understatement of the net amount payable with respect to any income tax, the penalty will not be asserted. However, if the error or omission results in a material understatement of the net amount payable with respect to any income tax, the partner generally will not be considered to have fully reported and the penalty will be applied.

SEC.4. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 81-11 is modified and superseded.

SEC. 5. EFFECTIVE DATE

This revenue procedure is effective for returns required to be filed after June 22, 1984.