



December 7, 2020

Ms. Holly Porter  
Associate Chief Counsel  
Passthroughs & Special Industries  
Internal Revenue Service  
1111 Constitution Ave, NW  
Washington, DC 20224

Ms. Holly Paz  
Director  
LB&I Passthrough Entities Practice Area  
Internal Revenue Service  
1111 Constitution Ave, NW  
Washington, DC 20224

**RE: [Draft Form 1065, U.S. Return of Partnership Income](#), [Draft Schedule K-1 \(Form 1065\), Partner's Share of Income, Deductions, Credits, etc.](#), and Related Instructions**

Dear Ms. Porter and Ms. Paz:

The American Institute of CPAs (AICPA) is pleased to submit suggestions on draft Form 1065, *U.S. Return of Partnership Income*, draft Schedule K-1 (Form 1065), *Partner's Share of Income, Deductions, Credits, etc.*, and related instructions. Our suggestions include comments and recommendations for your consideration as you work to update and finalize the 2020 Form 1065, Schedule K-1 (Form 1065), and related instructions.

### **Tax Basis Capital Account Suggestions**

#### **1. Sales & Exchanges**

- We recommend moving the discussion of transfers of capital to the “other increase/decrease” section of the instructions. Generally, transfers of capital in connection with sales or exchanges are presented as “an other increase/decrease” in each respective partner’s capital account. However, the current draft instructions discuss transfers of capital in the opening capital account section. This current placement is both confusing and misleading.

#### **2. Section 734 Adjustments**

- The current instructions discuss an approach to section 734 adjustments that could be read as inconsistent with the general framework as provided in our prior [comment letter](#).<sup>1</sup> We recommend removing the section 734 adjustments discussion and including the example we provided in our comment letter in a future FAQ release.

#### **3. Other Increase/Decrease Clarifications**

- We recommend clarifying that other increases and decreases include non-deductible expenses and tax-exempt income.

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<sup>1</sup> References to the [AICPA Comment Letter](#) are in regards to [Notice 2020-43](#) – Tax Capital Reporting.

- 4. Publicly Traded Partnerships (PTPs) & Section 743(b) Basis Adjustment Recovery**
  - We recommend including the recovery of section 743(b) basis adjustments in the current year income/loss effect on tax basis capital for item L with respect to PTPs that use transferee purchase price for beginning basis. This is in contrast to the general rule that excludes the recovery of section 743(b) basis adjustments from tax capital.
- 5. Reconciliations of Schedule M-2 to Schedule L Capital and Aggregate Item L Capital**
  - We recommend providing an example in the instructions to Form 1065, of how to reconcile Schedule M-2 to Schedule L and aggregate Item L capital. The examples should include common reconciling items.
- 6. Subsequent FAQ Example Release**
  - We recommend issuing an FAQ that includes the examples provided in our [comment letter](#) relating to section 734 adjustments, sales or exchanges, and “hanging negative” capital accounts.

### **Other General Suggestions**

- 1. Form 1065 Page 5, Line 1 – Net Income (Loss)**
  - We recommend updating Form 1065 to exclude guaranteed payment income from Net Income (Loss). The Page 5, Line 1 – Net Income (Loss) analysis is commonly interpreted as partnership net taxable income or (loss), and it is the starting point for numerous other calculations on the partnership tax return (e.g., partnership section 163(j) computations). Form 1065 indicates Net Income (Loss) is computed by combining Schedule K, lines 1 through 11 and subtracting from the result Schedule K, lines 12 through 13d, and 16p. However, the computation will not be representative of partnership taxable income or (loss) if the partnership has reported guaranteed payment income on Line 4 of Schedule K. While the *deduction* for guaranteed payments is properly included in partnership taxable income or (loss), guaranteed payment income is income to the recipient, *not* the partnership. As a result, guaranteed payment income will often be incorrectly included in capital accounts. To the extent updating the forms is not possible for the 2020 tax year, we recommend providing clarification in the instructions that tax capital accounts should not include guaranteed payment income.
  - We also recommend clarifying in the instructions that tax capital should not include the recovery of section 743(b) adjustments even though the adjustments are included in the computation of partnership net income (loss) previously described.

## 2. State Reporting Reference

- We recommend deleting the language “Any other information the partners need to prepare their tax returns, including information needed to prepare state and local tax returns” on page 53 of the Form 1065 draft instructions. The language is vague and given it is a new addition to the instructions, there is uncertainty of what additional information reporting is now required as compared to prior tax years.

## 3. PTPs & Section 704(c) Reporting

- We recommend removal of the requirement for PTPs to report ending section 743(b) information on Line 20AH given that PTPs are not required to report section 704(c) information or section 743(b) recovery on Lines 11F and 13V.

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We appreciate your consideration of these comments and welcome the opportunity to discuss these issues further. If you have any questions, please contact Sarah Allen-Anthony, Chair, AICPA Partnership Taxation Technical Resource Panel, at (574) 235-6818 or [Sarah.Allen-Anthony@crowe.com](mailto:Sarah.Allen-Anthony@crowe.com); Alexander Scott, AICPA Senior Manager – Tax Policy & Advocacy, at (202) 434-9204 or [Alexander.Scott@aicpa-cima.com](mailto:Alexander.Scott@aicpa-cima.com); or me at (612) 397-3071 or [Chris.Hesse@CLAconnect.com](mailto:Chris.Hesse@CLAconnect.com).

Sincerely,



Christopher W. Hesse, CPA  
Chair, AICPA Tax Executive Committee