California Regulation, Section 25137-1--[Reg. 25137-1. Apportionment and Allocation of Partnership Income.--

(a) In General.--When a taxpayer has an interest in a partnership as defined in Section 17008, Revenue and Taxation Code, the division of its distribute share of partnership items shall be determined in accordance with Chapter 10 of Part 10 of Division 2 of the Revenue and Taxation Code. The determination of the portion of such distributive share (constituting business and nonbusiness income) which has its source in this state or which is includible in the taxpayer's business income subject to apportionment, shall be made in accordance with these regulations provided that the taxpayer, or the partnership, or both, have income from sources within and without this state. The taxpayer in computing net income for its income year shall include its distributive share of partnership items referred to above for any partnership year ending within or with the taxpayer's income year.

The first step is to determine which portion of the taxpayer's income and its distributive share of the partnership items constitute “business income” and “nonbusiness income” under Section 25120, Revenue and Taxation Code, and the regulations thereunder. The various items of nonbusiness income are then directly allocated to specific states pursuant to the provisions of Section 25124 to 25127, Revenue and Taxation Code. The taxpayer's distributive share of partnership business income is apportioned by the formula set forth in subsections (f) or (g), whichever is applicable. The sum of (1) the items of nonbusiness income directly allocated to this state, plus (2) the amount of business income attributed to this state is the portion of the taxpayer's entire net income which is subject to tax.

Income arising from transactions and activity in the regular course of the partnership's trade or business constitutes business income. Thus, a corporate-partner's distributive share of partnership business income constitutes business income to the corporate-partner, but the determination of whether the partnership's activities and the activities of the corporate-partner constitutes a single trade or business or more than one trade or business turns on the facts in each case. If the partnership's activities and the taxpayer's activities constitute a unitary business under established standards, disregarding ownership requirements, the taxpayer's share of the partnership's trade or business shall be combined with the taxpayer's trade or business as constituting a single trade or business.

Example 1: Corporation A's distributive share of income in partnership P is 20%. Corporation A manufactures toys which are sold in the seven western states by partnership P. Corporation A's business income for the year was $1,000,000 and partnership P's business income for the same year was $800,000. The business income of Corporation A is $1,160,000 ($1,000,000 plus 20% of $800,000).

Example 2: Corporation A's distributive share of income in partnership P if 90%. Partnership P manufactures toys of which approximately 30% are sold by Corporation A in the seven western states. The remainder is sold to outsiders by partnership P. In addition, Corporation A also sells other lines of toys not manufactured by partnership P. Corporation A handles all financing, management, accounting, advertising, and purchasing functions for partnership P as well as for itself. Corporation A incurred a loss of $500,000 for the year but partnership P's income was $1,000,000. The business income of Corporation A is $400,000 (90% of $1,000,000 = $900,000 less the loss of $500,000).

When the activities of the partnership and the taxpayer do not constitute a unitary business under established standards, disregarding ownership requirements, the taxpayer's share of the partnership's trade or business shall be treated as a separate trade or business of the taxpayer. In such a case the taxpayer is engaged in two trades or businesses.

Example: Corporation A's distributive share of income in partnership P is 20%. Corporation A manufactures and sells toys in the seven western states. Partnership P operates farms within and without this state. Corporation A's income for the year is $1,000,000 and partnership P's income is $800,000 for the same year. Corporation A is engaged in two trades or businesses, and will be required to apportion its income of $1,000,000 from its own operations to this state on the basis of a three factor apportionment formula. Partnership P would attribute part of its business income of $800,000 to this state on the basis of its own three factor apportionment formula. Accordingly, Corporation A would report 20% of the partnership income apportioned to this state plus a portion of its income from its toy manufacturing business.

(b) Distributive Items of Nonbusiness Income.--Partnership income from interest, dividends, rents, royalties or capital gains is nonbusiness income when such income does not constitute business income. The taxpayer's distributive share of such nonbusiness income shall be reported in the same manner as other nonbusiness income derived from other activities of the taxpayer (see Section 25123 to 25127, inclusive).

(c) Business and Nonbusiness Income; Application of Definitions.--The classification of income by the labels customarily given such as interest, dividends, rents, royalties, capital gains, etc., is of no aid in determining whether partnership income is business or nonbusiness income. The gain or loss recognized on the sale of property, for example, may be business income or nonbusiness income depending upon the relation to the partnership's trade or business. Rules and examples for determining whether these types of income constitute business or nonbusiness income are set forth in Regulation 25120(c) and are applicable to partnerships under this regulation.

(d) Proration of Deductions.--In most cases an allowable deduction of a partnership will be applicable to the business income arising from a particular trade or business or to a particular item of nonbusiness income. In some cases an allowable deduction may be applicable to the business incomes of more than one trade or business and/or to several items of nonbusiness income. In such cases the deduction shall be prorated among such trades or businesses and such items of nonbusiness income in a manner which fairly distributes the deduction among the classes of income to which it is applicable.

(e) Distributive Items of Expense.--Any items of expense distributed to the taxpayer in accordance with Chapter 10 of Part 10 of Division 2 of the Revenue and Taxation Code, shall be taken into account in computing the taxpayer's business and nonbusiness income, to the extent allowable under the law and in accordance with these regulations as to determining their applicability to the taxpayer's business or nonbusiness income.

(f) Apportionment of Business Income--Single Trade or Business.--If the partnership's activities and the taxpayer's activities constitute a unitary business under established standards, disregarding ownership requirements, the business income of such single trade or business attributable to this state shall be determined by a three factor formula consisting of property, payroll and sales of the taxpayer and its share of the partnership's factors for any partnership year ending within or with the taxpayer's income year as follows:

(1) Property Factor. In general the numerator and denominator of the property factor shall be determined as set forth in Regulations 25129 to 25131, inclusive, and 25137(b). However, the following special rules shall apply:

(A) A portion of the partnership's real and tangible personal property, both owned or rented and used during the income year in the regular course of such trade or business, to the extent of the taxpayer's interest in the partnership, shall be included in the denominator of the taxpayer's property factor.

(B) The value of such property located in this state shall also be included in the numerator of the property factor. The value of property which is rented or leased by the taxpayer to the partnership or vice versa shall, with respect to the taxpayer, be excluded from the property factor of the partnership or eliminated to the extent of the taxpayer's interest in the partnership, whatever the case may be, in order to avoid duplication.

Example 1: Corporation A's interest in partnership P is 20%. Corporation A's distributive share of partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A owns a building (original cost of $100,000) which is rented to partnership P for $12,000 per year. Corporation A must include the original cost of $100,000 for the building in its property factor. Therefore, no portion of the value of the rented property will be reflected in the property factor of Corporation A.

Example 2: Same facts as in Example 1 except partnership P owns the building and rents it to Corporation A. Corporation A will include $20,000 (20% of $100,000) in its property factor because of its interest in partnership P. In addition, Corporation A will take into account $9,600 ($12,000 less 20% thereof) of rental expense into its property factor in order to give weight in the property factor to the rented building used in Corporation A's operation. Thus, the value of the building to be used in the property factor of Corporation A is $96,800 ($20,000 plus 8 x $9,600).

(2) Payroll Factor. In general the numerator and denominator of the payroll factor shall be
determined as set forth in Regulations 25132 and 25133. However, the following special rules shall apply:

(A) The partnership's payroll used to produce business income, shall be included in the denominator of the taxpayer's payroll factor to the extent of the taxpayer's interest in the partnership. The amount of any such payroll applicable to this state shall also be included in the numerator of the taxpayer's payroll factor.

Example 1: Corporation A's interest in partnership P is 20% and its distributive share of partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A's own payroll is $1,000,000 and the payroll of partnership P is $800,000. Corporation A's total payroll for purposes of the payroll factor is $1,160,000 ($1,000,000 plus 20% of $800,000).

(3) Sales Factor. In general the numerator and denominator of the sales factor shall be determined as set forth in Regulations 25134 to 25136, inclusive, and 25137(c). However, the following special rules shall apply:

(A) The partnership's sales which give rise to business income, shall be included in the denominator of the taxpayer's sales factor to the extent of the taxpayer's interest in the partnership. The amount of such sales attributable to this state shall also be included in the numerator of the taxpayer's sales factor. Intercompany sales between the partnership and the taxpayer shall be eliminated from the denominator and numerator of the taxpayer's sales factor as follows:

(i) Sales by the taxpayer to the partnership to the extent of the taxpayer's interest in the partnership.

(ii) Sales by the partnership to the taxpayer not to exceed the taxpayer's interest in all partnership sales.

(B) Notwithstanding any intercompany eliminations described in subparagraph (A) above, sales
made to nonpartners shall be included in the denominator of the taxpayer's sales factor in an amount equal to such taxpayer's interest in the partnership.

(C) Application of the above rules [is] illustrated by the following examples:

Example 1: Corporation A's interest in partnership P is 20%, and its distributive share of partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A's sales were $20,000,000 for the year, $5,000,000 of which were made to partnership P. Partnership P made sales of $10,000,000 during the same year, none of which were to Corporation A or the other partners.

The denominator of Corporation A's sales factor is $21,000,000 determined as follows:

Sales by Corporation A		$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	$2,000,000	
Less: Corporation A's interest (20%) in Corporation A's sales to Partnership P	1,000,000	1,000,000
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Denominator of Sales Factor		$21,000,000
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Example 2. The following facts are applicable to Examples 2(a) to (c), inclusive. Corporation A's interest in partnership P is 20% and Corporation B's interest is 80%. The distributive share of partnership income is included in business income of Corporation A and Corporation B, respectively.

(a) The sales made by Corporation A, Corporation B, and Partnership P are as follows:

Corporation A		$20,000,000
Corporation B		60,000,000
Partnership P:		
To Corporation A	$2,000,000	
To Corporation B	8,000,000	$10,000,000

The denominator of Corporation A's sales factor is $20,000,000 determined as follows:

Sales by Corporation A		$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	$2,000,000	
Less: Partnership P's Sales to Corporation A	2,000,000	--0--
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Denominator of Corporation A's sales factor		$20,000,000

The denominator of Corporation B's sales factor is $60,000,000 determined as follows:

Sales by Corporation B		$60,000,000
Add: Corporation B's interest (80%) in Partnership P's sales	$8,000,000	
Less: Partnership P's sales to Corporation B	8,000,000	--0--
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(b) The sales made by Corporation A, Corporation B, and Partnership P are as follows:

Corporation A		$20,000,000
Corporation B		60,000,000
Partnership P:		
To Corporation A	$1,000,000	

To Corporation B	9,000,000	$10,000,000

The denominator of Corporation A's sales factor is $21,000,000 determined as follows:

Sales by Corporation A		$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	$2,000,000	
Less: Partnership P's sales to Corporation A	1,000,000	1,000,000
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Denominator of Corporation A's sales factor		$21,000,000
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The denominator of Corporation B's sales factor is $60,000,000 determined as follows:

Sales by Corporation B		$60,000,000
Add: Corporation B's interest (80%) in Partnership P's sales	$8,000,000	
Less: Intercompany sales between Partnership P and Corporation B *	8,000,000	--0--
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Denominator of Corporation B's sales factor		$60,000,000
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(c) The sales made by Corporation A, Corporation B, and partnership P are as follows:

Corporation A		$20,000,000
Corporation B		80,000,000
Partnership P:		
To Corporation A	$3,000,000	
To Corporation B	6,000,000	
To Corporation X	1,000,000	$10,000,000

The denominator of Corporation A's sales factor is $20,200,000 determined as follows:

Sales by Corporation A		$20,000,000
Add: Corporation A's interest in Partnership P's sales to nonpartner X Corporation (20% x $1,000,000)		200,000

Corporation A's interest in Partnership P's sales to Partners (20% x $9,000,000)	$1,800,000	
Less: Intercompany sales from Partnership P to Corporation A *	1,800,000	--0--
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Denominator of Corporation A's sales factor		$20,200,000
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The denominator of Corporation B's sales factor is $81,800,000 determined as follows:

Sales by Corporation B		$80,000,000
Add: Corporation B's interest in Partnership P's sales to Nonpartners X Corporation (80% x $1,000,000)		800,000
Corporation B's interest in Partnership P's sales to Partners (80% x $9,000,000)	$7,200,000	
Less: Intercompany sales from Partnership P to Corporation B	6,000,000	1,200,000
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Denominator of Corporation B's sales factor		$82,000,000
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* Not to exceed taxpayer's interest in Partnership P's sales

(4) Partnership Interest--Defined. A taxpayer's partnership interest for the purpose of computing the portion of the partnership's property, payroll and sales to be included in the taxpayer's property, payroll or sales factor shall be determined under Chapter 10 of Part 10 of Division 2 of the Revenue and Taxation Code, and the regulations thereunder.

(5) Common Accounting Period. If a partnership and a corporation are engaged in a unitary business and their accounting periods are different, if necessary, in order to avoid distortion, the income and factors of the partnership will be determined on the basis of the corporate partner's accounting period.

(g) Apportionment of Business Income--Two or More Trades or Businesses.--When the activities of the partnership and the taxpayer do not constitute a unitary business under established standards, disregarding ownership requirements, the taxpayer's share of the partnership's trade or business shall be treated as another trade or business of the taxpayer. The determination of the amount of the partnership's business income and the taxpayer's distributive share of that income attributable to sources within this state shall be as follows:

(1) If the partnership derives business income from sources within and without this state, the amount of business income derived from sources within this state shall be determined on the basis of a three factor formula of property, payroll and sales. The factors shall be determined in accordance with the provisions of Section 25129 to 25137, inclusive, Revenue and Taxation Code, and the regulations thereunder. After determining the amount of business income attributable to this state by the three factor formula, the taxpayer's distributive share of such business income shall be reported as business income from a separate business by the taxpayer. That income when added to the taxpayer's other business income apportioned to this state and nonbusiness income allocable to this state is the taxpayer's measure of tax for its income year.

Example: Corporation A's distributive share of income in partnership P is 20%. Partnership P derives income from sources within and without this state but its business is unrelated to the business of Corporation A. Partnership P has business income of $500,000 for the year of which 40% is apportioned to this state by its three factor formula of property, payroll and sales. Corporation A shall include in its measure of tax its income received from partnership P $40,000 ($500,000 x 40% x 20%).

(2) If the partnership derives business income from sources entirely within this state, or entirely without this state, such income shall not be subject to formula apportionment. The taxpayer's distributive share of such business income attributable to this state (if any) shall be added to the taxpayer's other business income apportioned to this state plus nonbusiness income, if any, allocable to this state, the total of which is the taxpayer's measure of tax for its income year.

Example 1: Corporation A's distributive share of income in partnership P is 20%. The distributive share of P's business income is not an integral part of A's trade or business so as to be considered one business. Corporation A derives business income from sources within and without this state. Partnership P is engaged in business wholly within this state. Corporation A's business income for the year is $5,000,000 of which 50% is apportioned to this state. Partnership P has a loss on its operations for the same year of $500,000. Corporation A's measure of tax is $2,400,000 ($5,000,000 x 50% = $2,500,000 - $100,000 ($500,000 x 20%)).

Example 2: Same facts as in Example 1 except partnership P operates its business wholly outside this state. Corporation A's measure of tax is $2,500,000 ($5,000,000 x 50%) as no portion of partnership P's loss is attributable to this state.

(h) Apportionment of Business Income--Long-Term Construction Contracts.--If the partnership's activities and the taxpayer's activities constitute a unitary business under established standards, disregarding ownership requirements, so as to constitute a single trade or business and the partnership is engaged in long-term construction contracts and has elected either the percentage of completion method of accounting, or the completed contract method of accounting, the distributive share of partnership business income to be reported each year by the taxpayer shall be determined by reference to the preceding sections of this regulation where applicable and to the following subparagraphs regardless of whether the partnership's operations are carried on entirely within this state, entirely without this state, or partly within and partly without this state.

(1) Percentage of Completion Method. Under this method of accounting for long-term contracts the amount to be included each year as business income from each contract, is the amount by which the gross contract price which corresponds to the percentage of the entire contract which has been completed during the income year exceeds all expenditures made during the income year in connection with the contract. In so doing account must be taken of the material and supplies on hand at the beginning and end of the income year for use in such contract. Each corporate partner is required to report its distributive share of income as set forth in these regulations.

Example: A construction partnership using the percentage of completion method of accounting
for long-term contracts, entered into a long-term contract to build a structure for $9,000,000. The contract allowed three years for completion, and as of the end of the second partnership year the partnership's books of account, kept on the accrual method, disclosed the following:

	Receipts	Expenditures
End of 1st partnership year	$2,500,000	$2,400,000
End of 2nd partnership year	4,500,000	4,100,000
Totals	$7,000,000	$6,500,000

In computing the above expenditures, consideration was given to material and supplies on hand
at the beginning and end of each year.

It was estimated that the contract was 30% completed at the end of the first year and 80% completed at the end of the second year. The amount of business income for the first partnership year is $300,000 (30% of $9,000,000 or $2,700,000 less expenditures of $2,400,000). The amount of business income for the second partnership year is $400,000 (50% of $9,000,000 or $4,500,000 less expenditures of $4,100,000). Each year the corporatepartners would report their respective distributive shares of business income from the contract.

(2) Completed Contract Method. Under this method of accounting for long-term contracts a
special computation is required to apportion the distributive share of partnership income from each completed contract (see paragraph (6) of this regulation). Accordingly, all receipts and expenditures applicable to such contracts whether complete or incomplete as of the end of the income year are excluded from other types of business income, such

as interest, rents, royalties, etc., which are apportioned by the regular three factor formula of property, payroll and sales (see subsection (f) of this regulation).

(3) Property Factor. The numerator and denominator of the property factor shall be determined as set forth in subsection (f)(1) of this regulation subject to the following special rules.

(A) The taxpayer's interest in the average value of the partnership's cost (including materials and labor) of construction in progress, to the extent such costs exceed progress billings (accrued or received, depending on whether the partnership reports on the accrual or cash basis for keeping its accounts) shall be included in the denominator of the taxpayer's property factor. The value of any such property located in this state shall be included in the numerator of the taxpayer's property factor.

Example 1: A partnership started a long-term construction project in this state on the first day of the partnership's year. By the end of the second partnership year its equity in the costs of production for such year is computed as follows:

	1st Year Beginning	1st Year Ending	2nd Year Beginning	2nd Year Ending
Construction Costs	0	$1,000,000		
Progress Billings		600,000		
Balance		$ 400,000	$ 400,000	
Construction Costs--Total from Beginning of Project				$5,000,000
Progress Billings--Total from Beginning of Project				4,000,000
Balance End of Year				$1,000,000
Balance Beginning of Year				400,000
Total				$ 1,400,000
Average (1/2)				$ 700,000

Each corporate partner would include its respective share of $700,000 in its property factor based on its interest in the partnership.

Note: It may be necessary to use monthly averages if yearly averages do not properly reflect the average value of the partnership's equity (see Section 25131 and the regulations thereunder).

Example 2: Same facts as in Example 1, except that progress billings exceeded construction costs. No value for the corporate-partner's interest in the construction project is shown in its property factor.

(B) Rent paid for the use of equipment directly attributable to a particular construction project is included in the corporate-partner's property factor at eight times the net annual rental rate to the extent of its partnership interest even though such rental expense may be included in the cost of construction.

(C) The taxpayer's interest in partnership property for property factor purposes is computed in the same manner regardless of the long-term contract method of accounting elected and is
computed for each partnership year even though business income is computed separately under the completed contract method of accounting.

(4) Payroll Factor. The numerator and denominator of the payroll factor shall be determined as set forth in subsection (f)(2) of this regulation subject to the following special rules:

(A) Compensation paid employees which is attributable to a particular construction project is included in the payroll factor of the taxpayer to the extent of its partnership interest even though such compensation is included in the cost of construction.

(B) Compensation paid employees who in the aggregate perform most of their services in a state to which their employer does not report such employees for unemployment tax purposes, shall nevertheless be attributed to the state where the services are performed and shall be included in the numerator of the taxpayer's payroll factor to the extent of the taxpayer's interest in the partnership.

Example: A partnership engaged in a long-term contract in state X assigns several key employees to that state to supervise the project. The partnership, for unemployment tax purposes continues to report these employees to state Y where the partnership's main office is located and where the employees reside. For payroll factor purposes the compensation is included in the numerator for state X to the extent of the taxpayer's interest in the partnership.

(C) The taxpayer's interest in the partnership payroll is computed in the same manner for all long-term contract methods of accounting and is computed for each partnership year even though under the completed contract method of accounting, business income is computed separately.

(5) Sales Factor. The numerator and denominator of the sales factor shall be determined as set forth in subsection (f)(3) of this regulation subject to the following special rules:

(A) Gross receipts to the extent of the taxpayer's interest in the partnership derived from a contruction contract are attributable to this state if the construction project is located in this state. If the construction project is located partly within and partly without this state, gross receipts attributable to this state are based upon the ratio which construction costs for the project in this state for the year bears to the total of such construction costs for the entire project for the year.

Example: A partnership contracts to build a dam on a river at a point which lies half within this state and half within state X. During the first partnership year construction costs in this state are $2,000,000. Total construction costs for the project are $3,000,000 for the year. Gross receipts (progress billings) for the year are $2,400,000. Accordingly, gross receipts of $1,600,000 ($2,000,000/$3,000,000 = 66-2/3% x $2,400,000) are included in the numerator of the sales factor of the taxpayer to the extent of its partnership interest.

(B) If the percentage of completion method is used, the sales factor includes only that portion of the gross contract price which corresponds to the percentage of the entire contract which was completed during the partnership year to the extent of the taxpayer's partnership interest.

Example: A construction partnership which had elected the percentage of completion method of accounting entered into a long-term construction contract. At the end of its current year (the second since starting the project) it estimated that the project was 30% completed during the year. The bid price for the project was $9,000,000 and it had received $2,500,000 from progress billings as of the end of its current year. The amount of gross receipts for the current partnership year is $2,700,000 (30% of $9,000,000) regardless of whether the accrual method or the cash method for accounting for receipts and disbursements is used. The taxpayer will include a portion of such gross receipts in its sales factor to the extent of its partnership interest.

(C) If the completed contract method of accounting is used, the sales factor includes a portion of the gross receipts (progress billings) received or accrued, whichever is applicable, during the partnership year attributable to each contract to the extent of the taxpayer's partnership interest.

Example 1: A construction partnership which had elected the completed contract method of accounting entered into a long-term construction contract. By the end of its current year (the second since starting the project) it had billed, and accrued on its books a total of $5,000,000 of which $2,000,000 had accrued in the first year the contract was undertaken, and $3,000,000 had accrued in the current (second) year. The amount of gross receipts for the current partnership year is $3,000,000. The taxpayer will include a portion of such gross receipts in its sales factor to the extent of its partnership interest.

Example 2: Same facts as in Example 1 except that the partnership keeps its books on the cash basis, and as of the end of its current year had received only $2,500,000 of the $3,000,000 billed during the current year. The amount of gross receipts for the current partnership year is $2,500,000. The taxpayer will include a portion of such gross receipts in its sales factor to the extent of its partnership interest.

(D) The sales factor for each taxpayer except as noted above in subparagraphs (B) and (C), is computed in the same manner regardless of the long-term contract method of accounting elected by the partnership and is computed for each partnership year even though business income is computed separately under the completed contract method of accounting.

(6) Completed Contract Method--Special Computation. The completed contract method of accounting requires that the reporting of income (or loss) be deferred until the year the construction contract is completed and accepted. Accordingly, a separate computation is made for each such contract completed during the partnership year both within and without this state in order to determine the amount of distributive income which is attributable to sources within this state.

The amount of distributive income (or loss) from each contract which is derived from sources within this state using the completed contract method of accounting is computed as follows:

(A) In the partnership year the contract is completed the income (or loss) therefrom is computed and the taxpayer's distributive share determined.

(B) The taxpayer's distributive share of income (or loss) determined at (A) is apportioned to this state by the following method:

(i) A fraction is determined for each year the contract was in progress. The numerator is the taxpayer's partnership interest in construction costs paid or accrued each year the contract was in progress. The denominator is the total of all such construction costs for the project to the extent of the taxpayer's interest in the partnership.

(ii) Each percentage determined in (i) is multiplied by the taxpayer's apportionment formula percentage for that particular year as determined in subsection (f) and paragraphs (3), (4) and (5) above of this regulation.

(iii) The product determined at (ii) for each year the contract was in progress is totaled. The taxpayer's distributive share of income (or loss) on the contract determined at (A) is multiplied by the total percentage. The resulting income (or loss) is the amount of business income from such contract from sources within this state.

Example: The A corporation, engaged in long-term construction contracts, was also a partner in a construction partnership which elected to use the completed contract method of accounting for long-term contracts. The partnership was engaged in one long-term contract (Contract M in state X). During 1972 the partnership completed Contract M in state X at a profit of $900,000. The A corporation's distributive share of the profit is $300,000. The apportionment percentages of the taxpayer as determined in subsection (f) and paragraphs (3), (4) and (5) above of this regulation and the percentages of contruction costs as determined in subparagraph “(B)” above for each year Contract M in state X was in progress are as follows:

	1970	1971	1972
Apportionment percentages (A Corporation)	30%	20%	40%
Percentages of construction costs of Contract M each year to total construction costs to the extent of A Corporation's interest in the partnership	20%	50%	30%

The A corporation's distributive share of partnership income from Contract M attributable to this state for 1972 is $84,000 computed as follows:

	1970	1971	1972	Total
Apportionment Percentage	30%	20%	40%	
Percent of Construction Costs	20%	50%	30%	100%
Product	6.00%	10.00%	12.00%	28%

28% of $300,000 = $84,000

(i) Apportionment of Business Income--Long-Term Construction Contracts. If the activities of the partnership and the taxpayer do not constitute a unitary business under established standards, disregarding ownership requirements and the partnership is engaged in long-term construction contracts reporting income therefrom under the percentage of completion or completed contract method of accounting, the taxpayer's distributive share of partnership income (or loss) attributable to this state shall be determined as follows:

(1) When the partnership is engaged in a construction project entirely within this state, the determination of its business income shall be made in accordance with the method of accounting elected by the partnership for reporting income from long-term contracts and the taxpayer's distributive share shall be reported as business income from sources within this state derived from a separate trade or business.

(2) Where the partnership is engaged in construction both within and without this state, the determination of the amount of business income therefrom attributable to the taxpayer derived from sources within this state shall be made in accordance with the method of reporting for such long-term construction contract as elected by the partnership and as set forth in Section 25137-2 [Regulation 25137-2--CCH.] applicable to corporations engaged in long-term construction contracts, as if the partnership were a corporation.

(3) Where the partnership is engaged in a construction project entirely without this state, the determination of the taxpayer's distributive share of such business income shall be made as though the taxpayer were engaged in a separate trade or business, no portion of which is carried on within this state.

Note:
Authority cited: Section 26422, Revenue and Taxation Code.
Reference: Section 25137, Revenue and Taxation Code.

(Applicable for income years beginning after December 31, 1972; amended effective

March 27, 1985.)