Interested Parties Version as of 4/27/18 – Changes Accepted
Incorporating Changes Related to Partnership Pays Election
And Including Other Edits and Comments Throughout as of 6/25/18
DRAFT (WITHOUT SUGGESTED REGULATIONS)

Model Uniform Statute and Regulation for Reporting Adjustments to Federal Taxable Income and Federal Partnership Audit Adjustments

This draft was produced by a working group consisting of representatives of the Council On State Taxation (COST), Tax Executives Institute (TEI), the ABA Section of Taxation’s SALT Committee, the American Institute of CPAs (AICPA), the Institute for Professionals in Taxation (IPT) and the Master Limited Partnership Association (MLPA) as well as a work group set up by the MTC uniformity committee. As of this date, this draft has not been officially endorsed by these organizations.

This draft has been reformatted with line numbering as well as internal citations simplified and underlined to aid in the final review.

1 SECTION A. Definitions
2 The following definitions apply for the purposes of [this subdivision of the State Code]:
3   (1) "Administrative Adjustment Request" means an administrative adjustment request filed by a Partnership under IRC section 6227.
4   (2) "Audited Partnership" means a Partnership subject to a Partnership Level Audit resulting in a Federal Adjustment.
5   (3) "Corporate Partner" means a Partner that is subject to tax under [reference to State law].
6   (4) "Direct Partner" means a Partner that holds an interest directly in a Partnership or Pass-Through Entity.
7   (5) "Exempt Partner" means a Partner that is exempt from taxation under [reference to State law] [except on Unrelated Business Taxable Income].
8   (6) "Federal Adjustment" means a change to an item or amount determined under the Internal Revenue Code that is used by a Taxpayer to compute [State tax] owed whether that change results from action by the IRS, including a Partnership Level Audit, or the filing of an amended federal return, federal refund claim, or an Administrative Adjustment Request by the Taxpayer. A Federal Adjustment is positive

Drafting note: This portion of definition should only be used by the [State] if it taxes unrelated business income.
(7) "Federal Adjustments Report" includes methods or forms required by [State Tax Agency] for use by a Taxpayer to report Final Federal Adjustments, including an amended [State] tax return, information return, or a uniform multistate report.

(8) "Federal Partnership Representative" means the person the Partnership designates for the taxable year as the Partnership’s representative, or the person the IRS has appointed to act as the Federal Partnership Representative, pursuant to IRC section 6223(a).

(9) "Final Determination Date" means the following:

(a) Except as provided in Section A(9)(b) and (c), if the Federal Adjustment arises from an IRS audit or other action by the IRS, the Final Determination Date is the first day on which no Federal Adjustments arising from that audit or other action remain to be finally determined, whether by IRS decision with respect to which all rights of appeal have been waived or exhausted, by agreement, or, if appealed or contested, by a final decision with respect to which all rights of appeal have been waived or exhausted. For agreements required to be signed by the IRS and the Taxpayer, the Final Determination Date is the date on which the last party signed the agreement.

(b) For Federal Adjustments arising from an IRS audit or other action by the IRS, if the Taxpayer filed as a member of a [combined/consolidated return/report under State law], the Final Determination Date means the first day on which no related Federal Adjustments arising from that audit remain to be finally determined, as described in Section A(9)(a), for the entire group.

(c) If the Federal Adjustment results from filing an amended federal return, a federal refund claim, or an Administrative Adjustment Request, or if it is a Federal Adjustment reported on an amended federal return or other similar report filed pursuant to IRC section 6225 (c), the Final Determination Date means the day on which the amended return, refund claim, Administrative Adjustment Request, or other similar report was filed.

(10) "Final Federal Adjustment" means a Federal Adjustment after the Final Determination Date for that Federal Adjustment has passed.

(11) "Indirect Partner" means a Partner in a Partnership or Pass-Through Entity that itself holds an interest directly, or through another Indirect Partner, in a Partnership or Pass-Through Entity.

(12) "IRC" means the Internal Revenue Code of 1986, as codified at 26 United States Code.
States Code (U.S.C.) Section 1, et seq., [insert State’s current practice to incorporate IRC] and applicable regulations as promulgated by the U.S. Department of the Treasury.  

(13) “IRS” means the Internal Revenue Service of the U.S. Department of the Treasury.

(14) "Non-Resident Partner" means an individual, trust, or estate Partner that is not a Resident Partner.

(15) "Partner" means a person that holds an interest directly or indirectly in a Partnership or other Pass-Through Entity.

(16) "Partnership" means an entity subject to taxation under Subchapter K of the IRC.

(17) “Partnership Level Audit” means an examination by the IRS at the partnership level pursuant to Subchapter C of Title 26, Subtitle F, Chapter 63 of the IRC, as enacted by the Bipartisan Budget Act of 2015, Public Law 114-74, which results in Federal Adjustments.

(18) "Pass-Through Entity" means an entity, other than a Partnership, that is not subject to tax under [reference to State law imposing tax on C corporations or other taxable entities].

(19) "Reallocation Adjustment" means a Final Federal Adjustment resulting from a Partnership Level Audit or an Administrative Adjustment Request that changes the shares of one or more items of partnership income, gain, loss, expense, or credit allocated to Direct Partners. A positive Reallocation Adjustment means the portion of a Reallocation Adjustment that would increase federal income for one or more Direct Partners, and a negative Reallocation Adjustment means the portion of a Reallocation Adjustment that would decrease federal income for one or more Direct Partners [pursuant to Regulations under IRC section 6225].

(20) "Resident Partner" means an individual, trust, or estate Partner that has his or her domicile in or is a resident for tax purposes in [State] under [reference to state laws] for the relevant tax period.

(21) "Reviewed Year" means the taxable year of a Partnership that is subject to a Partnership Level Audit from which Federal Adjustments arise.

(22) “Taxpayer” means [insert reference to State definition] and, unless the context clearly indicates otherwise, includes a Partnership subject to a Partnership Level Audit or a Partnership that has made an Administrative Adjustment Request, as

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2 Drafting note: A State may need to address undefined terms. Suggested language – “To the extent terms used in this [article] are not defined in this Section or elsewhere in [citation to chapter in which this article is contained], it is the intent of the Legislature to conform as closely as possible to the terminology used in the amendments to the IRC pertaining to the comprehensive partnership audit regime as contained in the Bipartisan Budget Act of 2015, Public Law 114-74, as amended, and this [article] shall be so interpreted.”
well as a Tiered Partner of that Partnership.

(23) “Tiered Partner” means any Partner that is a Partnership or Pass-Through Entity.

(24) “Unrelated Business Taxable Income” has the same meaning as defined in IRC section 512.\(^3\)

SECTION B. Reporting Adjustments to Federal Taxable Income – General Rule

Except in the case of Final Federal Adjustments that are required to be reported by a Partnership and its Partners and Indirect Partners, using the procedures in Section C, and Final Federal Adjustments required to be reported for federal purposes under IRC section 6225(a)(2), a Taxpayer shall report and pay any [State] tax due with respect to Final Federal Adjustments arising from an audit or other action by the IRS or reported by the Taxpayer on a timely filed amended federal income tax return, including a return or other similar report filed pursuant to IRC section 6225(c), or federal claim for refund by filing a Federal Adjustments Report with the [State Tax Agency] for the Reviewed Year and, if applicable, paying the additional [State] tax owed by the Taxpayer no later than 180 days after the Final Determination Date.

Section C. Reporting Federal Adjustments – Partnership Level Audit and Administrative Adjustment Request

Except for adjustments required to be reported for federal purposes pursuant to IRC section 6225(a)(2) or Final Federal Adjustments arising from a Partnership Level Audit not reported on an amended federal return or other similar report under IRC section 6225(c), and adjustments Final Federal Adjustments arising from a Partnership Level Audit or an Administrative Adjustment Request filed by a Partnership under IRC section 6227 shall be reported as required under this section C.

(1) State Partnership Representative.

(a) With respect to an action required or permitted to be taken by a Partnership under this Section C and a proceeding under [reference to provisions for State administrative appeal or judicial review] with respect to that action, the State Partnership Representative for the Reviewed Year shall have the sole authority to act on behalf of the Partnership, and to the Partnership’s Direct Partners and Indirect Partners shall be bound by those actions.

(b) The State Partnership Representative for the Reviewed Year is the Partnership’s Federal Partnership Representative unless the Partnership designates in writing another person as its State Partnership Representative.

(c) The [State Tax Agency] may establish reasonable qualifications for and

\(^3\) Drafting note: This term should only be used by the [State] if it taxes unrelated business income.
procedures for designating a person, other than the Federal Partnership Representative, to be the State Partnership Representative.

(2) Reporting and Payment Requirements for Partnerships Subject to a Final Federal Adjustment and their Direct Partners.

Final Federal Adjustments subject to the requirements of this Section C, Except for Final Federal Adjustments except for those subject to a properly made election under Section C(3), Final Federal Adjustments resulting from a Partnership Level Audit or an Administrative Adjustment Request filed by a Partnership under IRC section 6227 shall be reported as follows:

(a) The Partnership shall, no later than 90 days after the Final Determination Date, No later than 90 days after the Final Determination Date, the Partnership shall:

(i) File a completed Federal Adjustments Report, including partner level information as required under [reference to State law], with [State Tax Agency]; and

(ii) Notify each of its Direct Partners of their distributive share of the Final Federal Adjustments along with any other information necessary for calculating the state tax in a manner as provided by the [State Tax Agency]; and

(iii) File an amended composite return for Direct Partners as required under [reference to State law] and/or an amended withholding return for Direct Partners as required under [reference to State law] and pay the additional amount due under [reference to State law(s)] that would have been due had the Final Federal Adjustments been reported properly as required.

(b) [Except as provided under State law for minimal tax liabilities], no later than 180 days after the Final Determination Date, each Direct Partner that is taxed under [reference to State law imposing tax on individuals, trusts, estates, C corporations, etc.] shall:

(i) File a Federal Adjustments Report reporting their distributive share of the adjustments reported to them under Section C(2)(a)(ii) as required under [reference to State laws]; and

(ii) Pay any additional amount of tax due as if Final Federal Adjustments had been properly reported, plus any penalty and interest due under [reference to State law] and less any credit for related amounts paid or withheld and remitted on behalf of the Direct Partner under Section C(2)(a)(iii).

4 DRAFTER’S NOTE: If the state adopts a de minimis rule as further set out in this model, then this section would need to be conditioned on a reference to that rule.
(3) Election – Partnership Pays. Subject to the limitations in Section C(3)(c), an Audited Partnership making an election under this Subsection (3) shall:

(a) No later than 90 days after the Final Determination Date, file a completed Federal Adjustments Report, including partner information and notify the [State Agency] that it is making the election under this Subsection (3);

(b) No later than 180 days after the Final Determination Date, pay an amount, determined as follows, in lieu of taxes owed by its Direct and Indirect Partners:

(i) Exclude from Final Federal Adjustments and any positive Reallocation Adjustments the distributive share of these adjustments made to an Direct Exempt Partner that is not Unrelated Business Taxable Income:

(ii) Exclude from Final Federal Adjustments and any positive Reallocation Adjustments the distributive share of these adjustments made to a Direct or Indirect Partner that has filed a Federal Adjustments Report and paid the [State] tax due, as required under Section B, for the distributive share of adjustments reported on a federal amended return or other similar report as required under IRC section 6225(c) to obtain a modification of federal tax owed;

(iii) For the total distributive shares of the remaining Final Federal Adjustments plus positive Reallocation Adjustments allocated to Direct Corporate Partners or Direct Exempt Partners subject to tax under [reference to State law] apportion and allocate such adjustments as provided under [reference to existing multi-state business activity allocation/apportion law or regulation], and multiply that the resulting amount by the highest tax rate under [reference to State law];

(iv) For the total distributive shares of the remaining Final Federal Adjustments plus positive Reallocation Adjustments allocated to Non-Resident Direct Partners subject to tax under [reference to State law applying to individuals and /or trusts], determine the amount of such adjustments which is [State] source income under [reference to existing non-resident partner sourcing law or regulation], and multiply this [State] source income the resulting amount by the highest tax rate under [reference to State law applying to individuals and/or trusts];

(v) For the total distributive shares of the remaining Final Federal Adjustments plus positive Reallocation Adjustments allocated to Tiered Partners:

(A) Determine the amount of such adjustments which is of a type that it would be subject to sourcing to the [State] source income under [reference to existing State rules for allocating/apportioning income of
non-resident partner sourcing law or regulation]; and then determine
the portion of this amount that would be sourced to the state applying
these rules]

(B) Determine the amount of such adjustments which is of a type
that it would not be subject to sourcing to the [State] source income un-
dered by a Nonresident Partner under [reference to existing State sourcing
law or regulation rules for income fully sourced based on a taxpayer’s res-
idency];

(C) Determine the portion of the amount determined of such ad-
justments in Section C(3)(b)(v)(B) which is [State] source income under
[reference to existing sourcing law or regulation for income fully sourced
based on a taxpayer’s residency] that can be established, under regulation
issued by [State Agency], to be properly allocable to non-resident in-
direct partners Nonresident Indirect Partners; or—Alternatively, a part-
ership may request a reduction adjustment using the can be excluded
under procedures for Modified Reporting and Payment Method allowed
under Paragraph (S).

(vi) Multiply the total of the amounts determined in Section
C(3)(b)(v)(A) and (B) reduced by the amount determined in Section
C(3)(b)(v)(C) by the highest tax rate under [reference to State law applying to
individuals and/or trusts];

(vii) For the total distributive shares of the remaining Final Federal Ad-
justments plus positive Reallocation Adjustments made to Resident
Direct Partners subject to tax under [reference to State law applying to individ-
uals and/or trusts], multiply that amount by the highest tax rate under
[reference to State law applying to individuals and/or trusts];

(viii) Add the amounts determined in Section C(3)(b)(ii), (iv), (vi), and
(vii).

(iv)(c) Final Federal Adjustments subject to this election exclude:

(i) The distributive share of Final Audit Adjustments including positive
Reallocation Adjustments that must be included in the unitary business in-
come of any Direct or Indirect Corporate Partner that the Audited Partnership
is reasonably aware is required to file a return separately or as a member of a
group as provided in [reference to State law]

(ii) Any Final Federal Adjustments resulting from an Administrative Ad-
justment Request;

(iii) Any portion of the Final Federal Adjustments reported or reportable

Comment [HH25]: This is the second piece (see above) which needs to be explicit.

Comment [HH26]: I believe the intent is to include the total of this amount, but reduced under clause (C) below.

Comment [HH27]: Unnecessary. See comment above.

Comment [HH28]: The use of "allocated" may be confusing in this context.

Comment [HH29]: Unnecessary. See comment above.

Comment [HH30]: Not sure this is what we mean—or do we mean that the partnership is reasonably aware that the income is being allocated to the corporate partner?
on the Audited Partnership’s Federal Partnership Tax Return for the adjustment year as required under IRC section 6225 and the regulations thereunder.

(c)(d) {OPTIONAL PROVISIONS}

Option A - An Audited Partnership not otherwise subject to any reporting or payment obligation to [State] that makes an election under this Subsection (3) consents to be subject to [State] laws related to reporting, assessment, payment, and collection of [State] tax calculated under the election.

Option B - An Audited Partnership not otherwise subject to any reporting or payment obligation to [State] may not make an election under this Subsection (3).

(4) Tiered Partners. Each Tiered Partner and each Indirect Partner of an Audited Partnership that reported Final Federal Adjustments pursuant to Section C(2)(a)(ii) shall be subject to the applicable election, reporting and payment requirements for Audited Partnerships and their Direct Partners under this Section C, notwithstanding the interim time requirements in Subsections (2) and (3), and all reports and payments required to be made by such Partners under this Section C shall be completed within 90 days after the time for filing and furnishing statements to Tiered Partners and their Partners as established by the IRS under IRC section 6226 and the regulations thereunder. The Direct and Indirect Partners of an Audited Partnership that are Tiered Partners, and all of the Partners of those Tiered Partners that are subject to tax under [reference to State laws imposing tax on individuals, trusts, corporations, etc.] are subject to the reporting and payment requirements of Section C(2) the Tiered Partners are entitled to make the elections provided in Section C(3) and (5). The [State Agency] may promulgate regulations to establish procedures and interim time periods for the reports and payments required by Tiered Partners and Indirect their Partners and for making the elections under this Section C. In no case shall the Tiered Partners or their Partners be required to make any reports or payments until 90 days after the time for filing and furnishing statements to Tiered Partners and their Partners as established under IRC section 6226 and the regulations thereunder.

(5) Modified Reporting and Payment Method. Under procedures adopted by and Subject-subject to the approval of the [State Agency], an Audited Partnership or Tiered Partner may enter into an agreement with the [State Agency] to utilize an alternative reporting and payment method, including applicable time requirements or any other provision of this Section C, if the Audited Partnership or Tiered Partner demonstrates that the requested method will reasonably provide for the reporting and

Comment [HH31]: See comment in the introduction to Section C above.

Comment [HH32]: This needs to be explicit, I think.

Comment [HH33]: I think this may better express what we’re going for, but I’m not sure.

Comment [HH34]: I think we should be explicit here that there will need to be some procedures set out by the agency for doing this.
payment of taxes, penalties, and interest due under the provisions of this Section C. Application for approval of an alternative reporting and payment method must be made by the Audited Partnership or Tiered Partner within the time for election as provided in Section C(3) or (4), as appropriate.

(6) Effect of Election by Audited Partnership or Tiered Partner and Payment of Amount Due.

(a) The election made pursuant to Section C(3) or (5) is irrevocable, unless [State Agency], in its discretion, determines otherwise.

(b) If properly reported and paid by the Audited Partnership or Tiered Partner, the amount determined in Section C(3)(b), or similarly under an optional election under Section C(5), will be treated as paid in lieu of taxes owed by its Direct and Indirect Partners, to the extent applicable, on the same Final Federal Adjustments. The Direct Partners or Indirect Partners may not take any deduction or credit for this amount or claim a refund of the amount in this State. Nothing in this Subsection(C)(6) shall preclude a Direct Resident Partners from claiming a credit against taxes paid to this State pursuant to [reference to State law], any amounts paid by the Audited Partnership or Tiered Partners on the Resident Partner’s behalf to another state or local tax jurisdiction in accordance with the provisions of [State law or regulation allowing credit for taxes paid to another state or locality].

(7) Failure of Audited Partnership or Tiered Partner to Report or Pay.

Nothing in this Section C prevents the [State Agency] from assessing Direct Partners or Indirect Partners for taxes they owe, using the best information available, in the event that a Partnership or Tiered Partner fails to timely make any report or payment required by this Section C for any reason.

SECTION D. De Minimis Exception

The [State Agency] at its discretion may promulgate regulations to establish a de minimis amount upon which a taxpayer shall not be required to comply with Sections B and C of this [Chapter].


The [State Agency] will assess additional tax, interest, and penalties arising from Final Federal Adjustments arising from an audit by the IRS, including a Partnership Level Audit, or reported by the Taxpayer on an amended federal income tax return or as part of an Administrative Adjustment Request by the following dates:

(1) Timely Reported Federal Adjustments. If a Taxpayer files with the [State Agency] a Federal Adjustments Report or an amended [State] tax return as required
within the period specified in Sections B or C, the [State Agency] may assess any amounts, including in-lieu-of amounts, taxes, interest, and penalties arising from those Federal Adjustments if [State Agency] issues a notice of the assessment to the Taxpayer no later than:

(a) The expiration of the limitations period specified in [citation to State statute setting forth normal limitations period]; or

(b) The expiration of the one (1) year period following the date of filing with the [State Agency] of the Federal Adjustments Report.

(2) **Untimely Reported Federal Adjustments.** If the Taxpayer fails to file the Federal Adjustments Report within the period specified in Sections B or C, as appropriate, or the Federal Adjustments Report filed by the Taxpayer omits Federal Adjustments or understates the correct amount of tax owed, the [State Agency] may assess amounts or additional amounts including in-lieu-of amounts, taxes, interest, and penalties arising from the Final Federal Adjustments, if it mails a notice of the assessment to the Taxpayer by a date which is the latest of the following:

(a) The expiration of the limitations period specified in [citation to State statute setting forth normal limitations period]; or

(b) The expiration of the one (1) year period following the date the Federal Adjustments Report was filed with [State Agency]; or

(c) Absent fraud, the expiration of the six (6) year period following the Final Determination Date.

**SECTION F. Estimated [State] Tax Payments During the Course of a Federal Audit**

A Taxpayer may make estimated payments to the [State Agency], following the process prescribed by the [State Agency], of the [State] tax expected to result from a pending IRS audit, prior to the due date of the Federal Adjustments Report, without having to file the report with the [State Agency]. The estimated tax payments shall be credited against any tax liability ultimately found to be due to [State] (“Final [State] Tax Liability”) and will limit the accrual of further statutory interest on that amount. If the estimated tax payments exceed the final tax liability and statutory interest ultimately determined to be due, the Taxpayer is entitled to a refund or credit for the excess, provided the Taxpayer files a Federal Adjustments Report or claim for refund or credit of tax pursuant to [citation to State statute setting forth claim for refund requirements] no later than one year following the Final Determination Date.

**SECTION G. Claims for Refund or Credits of Tax Arising from Final Federal Adjustments Made by the IRS**

Notwithstanding the reporting requirement contained in Sections B or C, a Taxpayer may file a claim for refund or credit of tax arising from Federal Adjustments made by
the IRS on or before the later of:
(1) The expiration of the last day for filing a claim for refund or credit of [State] tax
pursuant to [citation to State statute setting forth claim for refund requirements],
including any extensions; or
(2) One year from the date a Federal Adjustments Report prescribed in Sections B
or C, as applicable, was due to the [State Agency], including any extensions pursuant to
Section G.
The Federal Adjustments Report shall serve as the means for the Taxpayer to report
additional tax due, report a claim for refund or credit of tax, and make other
adjustments (including to its net operating losses) resulting from adjustments to the
Taxpayer’s federal taxable income.

SECTION H. Scope of Adjustments and Extensions of Time.
(1) Unless otherwise agreed in writing by the Taxpayer and the [State Agency],
any adjustments by the [State Agency] or by the Taxpayer made after the expiration of
the [State’s normal statute of limitations for assessment and refund] is limited to
changes to the Taxpayer’s tax liability arising from Federal Adjustments.
(2) The time periods provided for in [this subdivision of the State Code] may be
extended:
   (a) Automatically, upon written notice to [State agency], by 60 days for an
Audited Partnership or Tiered Partner which has [10,000] or more Direct Part-
ners; or
   (b) By written agreement between the Taxpayer and the [State Agency] [pur-
suant to any regulation issued under this Section].
(3) Any extension granted under this Section G for filing the Federal Adjustments
Report extends the last day prescribed by law for assessing any additional tax arising
from the adjustments to federal taxable income and the period for filing a claim for
refund or credit of taxes pursuant to [citation to State statute setting forth claim for
refund requirements].

SECTION I. Effective Date
The amendments to this [section/chapter] applies to any adjustments to a Taxpayer’s
federal taxable income with a Final Determination Date occurring on and after [date].