

State Taxation of Partnerships – Status Report

UNIFORMITY COMMITTEE MEETING
NOVEMBER 10, 2026

BACKGROUND

REVIEW OF HOW WE GOT HERE

IMPORTANT CONTEXT

- States conform to Subchapter K's pass-through system –
  - Partnerships –
    - Recognize and characterize items
    - Report to partners necessary tax information
  - Partners –
    - Recognize their distributive share of items
    - Correctly report and pay their tax
- Attribution is the foundation of this system –
  - Partners are taxed as if they recognized the items of income directly from the source. IRC Sec. 702(b).

IMPORTANT HISTORY

- Withholding –
  - 1986 –
    - Congress proposed and enacted requirements for withholding on partnership income for foreign partners.
  - 1990 to 2003 –
    - MTC worked to adopt uniform withholding for non-resident partners despite arguments that –
      - States lacked nexus over those partners or
      - Income of passive partners was only taxable in the state of residence.
  - Today – states have withholding

IMPORTANT HISTORY

- Partnership-level treatment –
  - 2015 –
    - Congress recognized the partnership tax gap was bigger than other tax gaps, and
    - Imposed partnership-level audits and tax adjustments under the Bipartisan Budget Act.
  - 2017 –
    - Congress capped the SALT deduction, and
    - States adopted PTE taxes, which the IRS has informally blessed.

PERSISTENT MISTAKES

- Mistake – Treating partnership distributive share like a dividend.
  - Distributions and distributive share are separate.
  - Distributions may or may not be made in any given year.
  - Distributive share is the share of partnership income recognized by partners each year.
  - Distributions are not taxable – distributive share is.

PERSISTENT MISTAKES

- Mistake – Assuming that sourcing depends on the partner's role.
  - Federal rules impute U.S.- sourced income to foreign partners regardless of their role.
  - State rules also source income based on that income's character and the activities giving rise to it.
  - Example – there is no UDITPA rule for allocating partnership distributive share as a separate category.

ROLE OF COMPLEXITY

- Most partnerships are small, simple structures.
- Most income is generated by large, complex partnerships.
- Larger partnership structures may be the result of –
  - Providing investment and funding, including private equity investments.
  - Deliberate complexity to obscure or shift income.
- Large partnership structures are a choice made by the parties involved and that complexity comes with additional administrative cost – including administering the pass-through tax system.

PROCESS

HOW THE PROJECT HAS PROGRESSED

PRIMARY GOALS

- Consistency with –
  - Subchapter K
  - Treatment of business income generally
  - Entity-level taxes (withholding, composite, PTE taxes)
- Uniformity in sourcing to avoid –
  - Multiple taxation
  - Nowhere taxation
  - Income shifting

ISSUE OUTLINE

- General categories –
  - Nexus
  - Tax base
  - Sourcing
  - Credits
  - Sale of a partnership interest
  - Administration and enforcement

See https://mtc.gov/wp-content/uploads/2024/12/Partnership-Outline-January-1-2025.pdf

ISSUE FOCUS

- Work group decides which issues to focus on and has studied –
  - Investment partnerships
  - Guaranteed payments for services
  - Sourcing income in complex structures

ADDRESSING ISSUES

- Steps –
  - Review existing state rules
  - Evaluate approaches for consistency and uniformity
  - Capture information, findings, and general recommendations in a white paper
  - Draft model provisions

Throughout this process the work group takes state and public input and reports status to the Uniformity Committee

DRAFTING CHALLENGES

- States embed partnership rules into corporate and personal income tax sections.
- States often use different terminology for similar concepts.
- Current state rules may differ in their level of detail.

OTHER NOTES ON THE MODEL

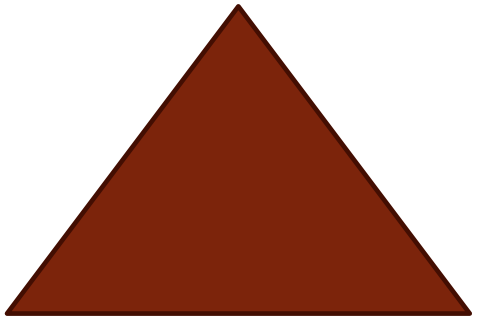
- Level of detail –
  - Provisions are generally drafted at a high level (whether in statutory or regulatory form).
- Use of existing sourcing rules –
  - Provisions refer to the state's existing sourcing rules and provide how these rules will be applied to partnership income.
- Authority granted to revenue agencies –
  - Provisions give agencies authority to issue guidance and require reporting – which is critical to the functioning of the system.

GENERAL SOURCING FRAMEWORK

AS SET OUT IN WHITE PAPERS AND DRAFT MODELS AND DISCUSSED THROUGHOUT THE PROCESS

GENERAL SOURCING FRAMEWORK

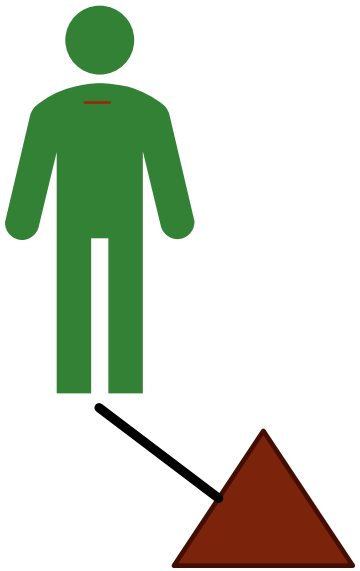
STARTING WITH THE OPERATING PARTNERSHIP



- Partnership determines and conveys information to direct partners –
  - Tax character of items recognized under substantive tax rules
  - Tax character of items recognized under state sourcing rules –
    - Whether items are apportionable or non-apportionable
    - If apportionable – the related state apportionment factors
    - If non-apportionable – what rules apply to specific items
  - Other information necessary for partners to comply with state tax laws

GENERAL SOURCING FRAMEWORK

DIRECT NON-RESIDENT PARTNERS

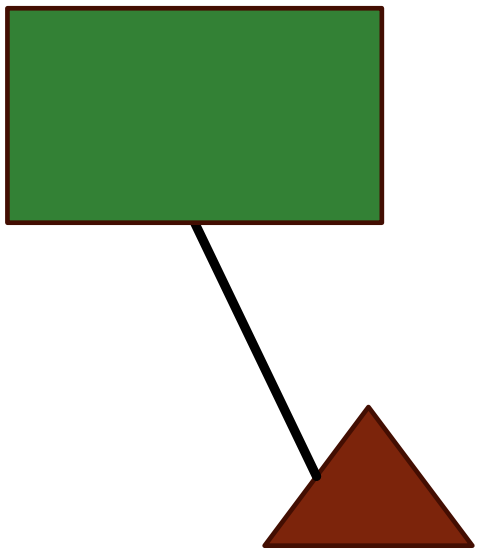


- Source distributive share of partnership items and guaranteed payments for services using partnership information.
  - It does not matter whether the partner is –
    - Active or passive
    - General or limited

Note that because some states tax guaranteed payments based on where the services are performed, the rules would also have the state of residence provide a credit for taxes paid on that basis.

GENERAL SOURCING FRAMEWORK

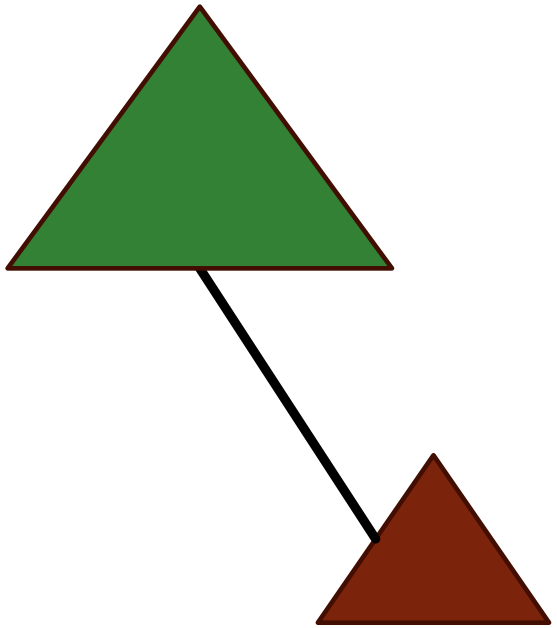
DIRECT CORPORATE PARTNERS



- Determine if there is a sufficient unitary relationship with partnership activities.
  - If not – source the same as direct nonresident partners.
  - If so –
    - Determine if any items treated as non-apportionable by the partnership are actually apportionable to the partner.
    - Use blended apportionment for apportionable items.

GENERAL SOURCING FRAMEWORK

TIERED PARTNERS



- Partnership determines and conveys information to direct partners on –
  - Sourcing of partnership's own income—using rules for operating partnerships.
  - Sourcing of partnership's income from lower tiers—using rules for direct corporate partners, except if the tiered partner is a qualified investment partnership.
    - If so – non-resident investment partners source items flowing from assets and operating partnerships as if that partner held the asset or interest directly.

DRAFT MODEL PROVISIONS

OVERVIEW – PROVISIONS AS SET OUT IN SEPTEMBER 15, 2026 REVISED DRAFT

PART I – DEFINITIONS

Partnership terms may have multiple sources of "definition"

- General state law governing partnerships
- Federal tax law – including Subchapter K
- State tax law

Terms that may be defined and used differently need explicit definitions to avoid ambiguity.

Also – definitions can help make explicit how the general framework of Subchapter K and the state sourcing rules work together.

DEFINITIONS – PART I (IMPORTANT EXAMPLES)

(l) Allocate or allocation of distributive share of income or items of income – A partnership's determination of a partner's share of partnership income or items of income under the partnership agreement as well as under any applicable state or federal tax law. See IRC § 704.

This is to distinguish the term "allocate" when used for partnership distributive share versus when used for sourcing generally.

DEFINITIONS – PART I (IMPORTANT EXAMPLES)

(21) Specifically assign and rules of assignment – The method used to source or allocate income or items of income under [REFERENCE(S) TO STATE STATUTORY PROVISIONS FOR SOURCING NON-APPORTIONABLE OR "NONBUSINESS" ITEMS OF INCOME.]

Adopting this term to distinguish "allocating" partnership income from "allocating" income for state sourcing purposes may be a difficult thing for states to do. It may be sufficient to look to the context of the use of the term "allocate."

DEFINITIONS – PART I (IMPORTANT EXAMPLES)

(23) Tax character of an item – The nature and classification of items for tax purposes which may affect their income tax treatment as determined by a partnership applying general substantive federal or state tax law based on the activity giving rise to the item. See IRC §§ 702(b) and 703(a) . . . . The tax character of an item may include:

a. The nature of receipts or expense – such as interest, royalties, dividends, gains (losses), etc.;

b. The type of transaction or activity giving rise to the income or expense – such as sales or purchases of property, leases of property, sales or purchases of services, depreciation of assets, borrowing of funds, etc.; and

c. The assets affected by the transaction or activity – such as real property, tangible or intangible property, inventory, etc.

This makes clear what "character" is and how it is determined generally.

DEFINITIONS – PART I (IMPORTANT EXAMPLES)

(4) Attribute (verb) or attribution of income or items – The way in which IRC Subchapter K and the pass-through system for partnerships which it creates assigns partnership items, as determined by the partnership recognizing those items, to any direct or indirect partners who are allocated a share of those items, without altering their tax character. This includes the tax character of these items that may affect the sourcing of the items under [REFERENCE(S) TO THE STATE'S STATUTORY PROVISIONS . . . .

This makes explicit that the partnership determines the character of income that affects sourcing and attributes that to the partners.

DEFINITIONS – PART I (IMPORTANT EXAMPLES)

(24) Taxpayer or partner attribute (noun) – An aspect of, or circumstance relating to a particular taxpayer that may affect the ultimate tax result for items recognized by or attributed to that taxpayer, which may include:

(a) Whether the taxpayer or partner is a resident or nonresident individual or a corporation or other type of entity;

(b) Whether the taxpayer or partner files a separate, joint, or combined/consolidated return;

(c) The taxpayer's marginal effective tax rate; and

(d) The taxpayer's participation or role in certain activities.

This distinguishes the use of "attribute" as a noun when applied to taxpayers.

PART II
CONFORMITY

- As discussed, conformity to Subchapter K means conformity to the attribution principle.
- Tax character of items is determined at the partnership level based on the assets or activities generating those items.
- Tax character or attributes of income also determine sourcing.
- States can be explicit about what conformity means.

CONFORMITY – PART II

(A) [STATE] conforms to the federal income tax law, including IRC Subchapter K, as provided in [REFERENCE(S) . . .. In conforming to Subchapter K, [STATE] also conforms to the principle that the tax character of items of income and loss is determined at the partnership level and then attributed to the partners who receive a distributive share of those items. This character as determined at the partnership level may affect the state income tax treatment of the items under the state income tax rules, including the sourcing of those items under [REFERENCE(S) TO STATE LAW FOR SOURCING INCOME . . ..

(B) In addition, [STATE] conforms to certain anti-abuse rules under IRC Subchapter K as described further in Part V of this Section.

PART III INFORMATION REPORTING

- Without proper information reporting the pass-through system is entirely unworkable.
- Federal tax rules require information reporting generally as well as consistency in reporting by partners and partnerships.
- Federal statutes provide the IRS with authority to require necessary reporting which is done through regulations and instructions.

OBLIGATIONS OF PARTNERSHIPS TO FILE INFORMATION RETURNS AND REPORT INFORMATION – PART III

(A) A partnership shall provide to its direct partners or beneficial interest holders the information necessary for its direct and indirect partners to properly compute and report their [STATE] tax. Necessary information includes any information as described or provided for in regulations, forms, and instructions issued by the [STATE TAX AGENCY]. This requirement to provide information applies to:

(1) Any partnership doing business in [STATE];

(2) Any partnership that has a direct or indirect partner or beneficial interest holder doing business in or resident in [STATE].

(3) Any partnership that has a direct or indirect interest in a partnership or other pass-through entity doing business in [STATE].

OBLIGATIONS OF PARTNERSHIPS TO FILE INFORMATION RETURNS AND REPORT INFORMATION – PART III (CONT'D)

(B) A partnership shall provide to the [STATE TAX AGENCY] certain information as directed by the [STATE TAX AGENCY] necessary to verify the information required to be reported to partners under Subpart A, above and as provided in regulations, forms, and instructions issued by the [STATE TAX AGENCY].

OBLIGATIONS OF PARTNERSHIPS TO FILE INFORMATION RETURNS AND REPORT INFORMATION – PART III (CONT'D)

(C) The type of information that may be required to be reported to partners or to [STATE TAX AGENCY] under this Part II includes:

1. Federal tax-related information, including the tax character of partnership income and items recognized by the partnership or allocated to the partnership from lower-tier partnerships;

2. State tax-related information, including the tax character of partnership income and items recognized by the partnership or allocated to the partnership from lower-tier partnerships, as relevant to compliance with [REFERENCE TO STATE INCOME TAX RULES FOR CORPORATIONS AND INDIVIDUALS];

OBLIGATIONS OF PARTNERSHIPS TO FILE INFORMATION RETURNS AND REPORT INFORMATION – PART III (CONT'D)

3. Information necessary for direct or indirect partners to properly determine the source of partnership income and items, as described further in this Section;

4. Information from lower-tier partnerships or business entities in which the partnership holds an interest that is necessary for that partnership's direct or indirect partners to properly determine the source of partnership income and items as described further in this Section; and

5. Any other information the partnership may have or obtain that is necessary for direct or indirect partners to properly report their state tax on partnership income and items.

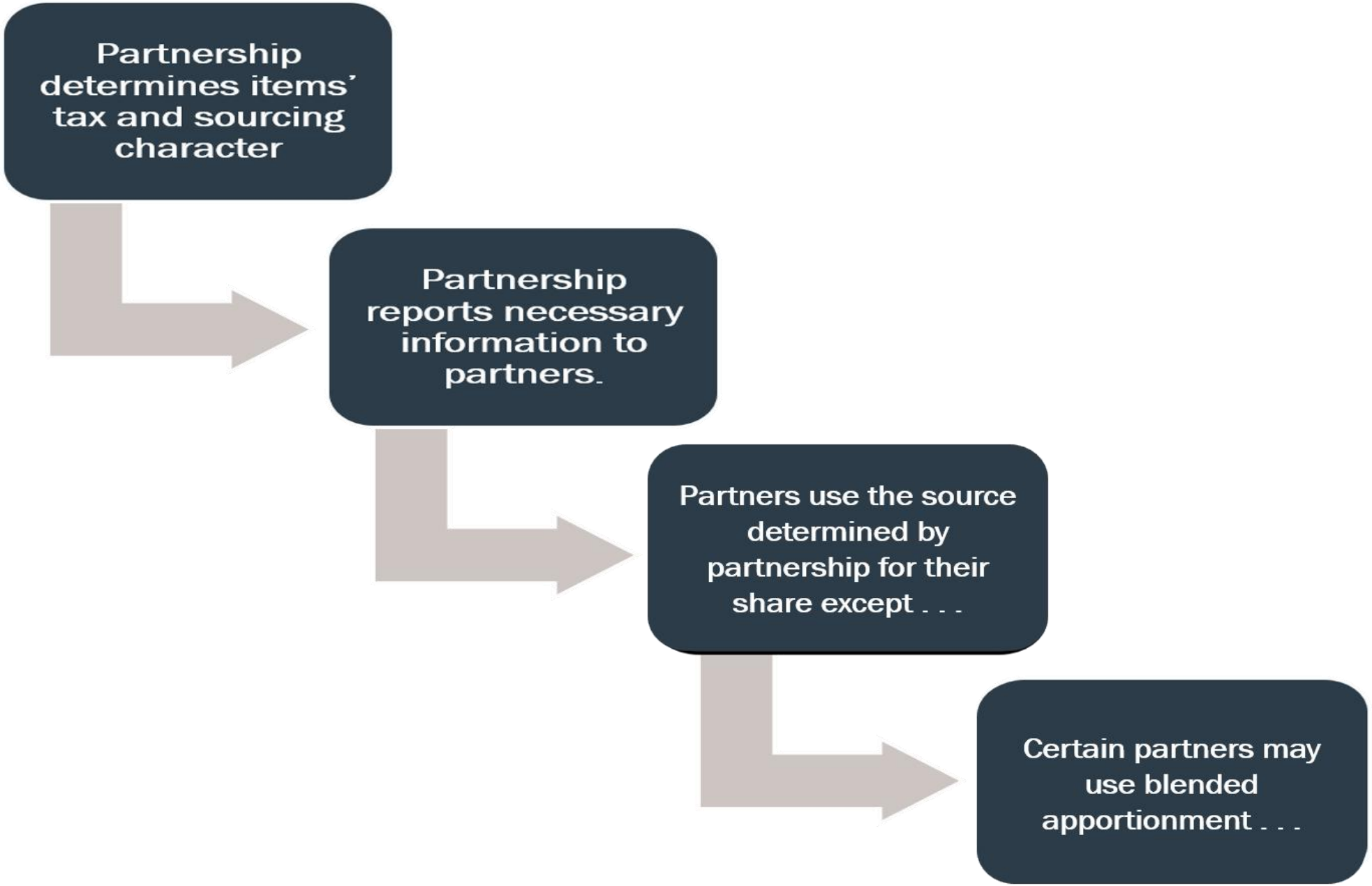
OBLIGATIONS OF PARTNERSHIPS TO FILE INFORMATION RETURNS AND REPORT INFORMATION – PART III (CONT'D) – NEW PROVISIONS

(D) To the beneficial interest holders of another pass-through entity that are taxed on partnership income flowing through that entity, the entity may also be required to report information described in this Part III.

(E) A partnership or other pass-through entity is presumed to have knowledge that an indirect partner or beneficial interest holder is doing business or resident in this state for purposes of this Part III if that information is otherwise known to that partnership or if the partnership has received a notification from a partner, indirect partner, or beneficial interest holder. If, under the circumstances, a partnership or other pass-through entity is not presumed to have this knowledge, the failure to provide information to its partners that is necessary for indirect partners or beneficial interest holders to properly compute and report their [STATE] tax will not be subject to any penalties.

PART IV SOURCING RULES

- The model provisions now cover sourcing for non-resident partners as well as where there are tiered or corporate partners.
- The model provisions include two special rules for:
  - Income of investment partnerships and
  - Guaranteed payments for services paid to individual partners.
- Those provisions have been reviewed in the past and we have responded to various comments.


Partnership determines items' tax and sourcing character
Partnership reports necessary information to partners.
Partners use the source determined by partnership for their share except . . .
Certain partners may use blended apportionment . . .

SOURCING PARTNERSHIP INCOME AND ITEMS – PART IV

(A) In applying the sourcing rules below, a partnership required to report information as described in Part III, must properly apply the applicable [STATE] and federal tax rules as required by Part II in determining that information.

(B) Items Recognized Directly by a Partnership:

Application of the rules for sourcing income under [REFERENCE TO STATE'S SOURCING RULES FOR INCOME OF BUSINESS ENTITIES, CORPORATIONS, OR NONRESIDENTS] to partnership income and items requires that a partnership determine the following with respect to the items of income, expense, gain, loss or other tax items that it recognizes directly from its activities and to guaranteed payments made to partners:

SOURCING PARTNERSHIP INCOME AND ITEMS – PART IV – (CONT'D)

(1) Information as to the general tax character of those partnership items as it may be relevant to state tax treatment of the items, including::

a. The tax character of the items for purposes of determining their federal tax treatment to which the state conforms;

b. The tax character of the items for purposes of determining their state tax treatment, including any treatment that varies from the federal tax treatment; and

c. The tax character of the items for purposes of applying the sourcing rules in [REFERENCE TO STATE'S SOURCING RULES FOR INCOME OF BUSINESS ENTITIES, CORPORATIONS, OR NONRESIDENTS].

SOURCING PARTNERSHIP INCOME AND ITEMS – PART IV – (CONT'D)

(2) Information as to whether any partnerships items are non-apportionable as that term is defined by this Section and the rules provided in [REFERENCES TO STATE'S SOURCING RULES—TREATMENT OF NON-APPORTIONABLE OR NONBUSINESS ITEMS FOR CORPORATIONS OR NONRESIDENTS] applying those rules based on:

a. The item's particular tax character as determined by the partnership; and

b. The relationship of the item to the business activity conducted by the partnership, alone or in conjunction with the activity conducted by one or more entities in which the partnership holds a direct or indirect interest.

In determining this information, the partnership must also determine whether its items of income have a sufficient unitary relationship to any business in which the partnership participates that also generates apportionable income, with the understanding that a partnership may engage in more than one unitary business.

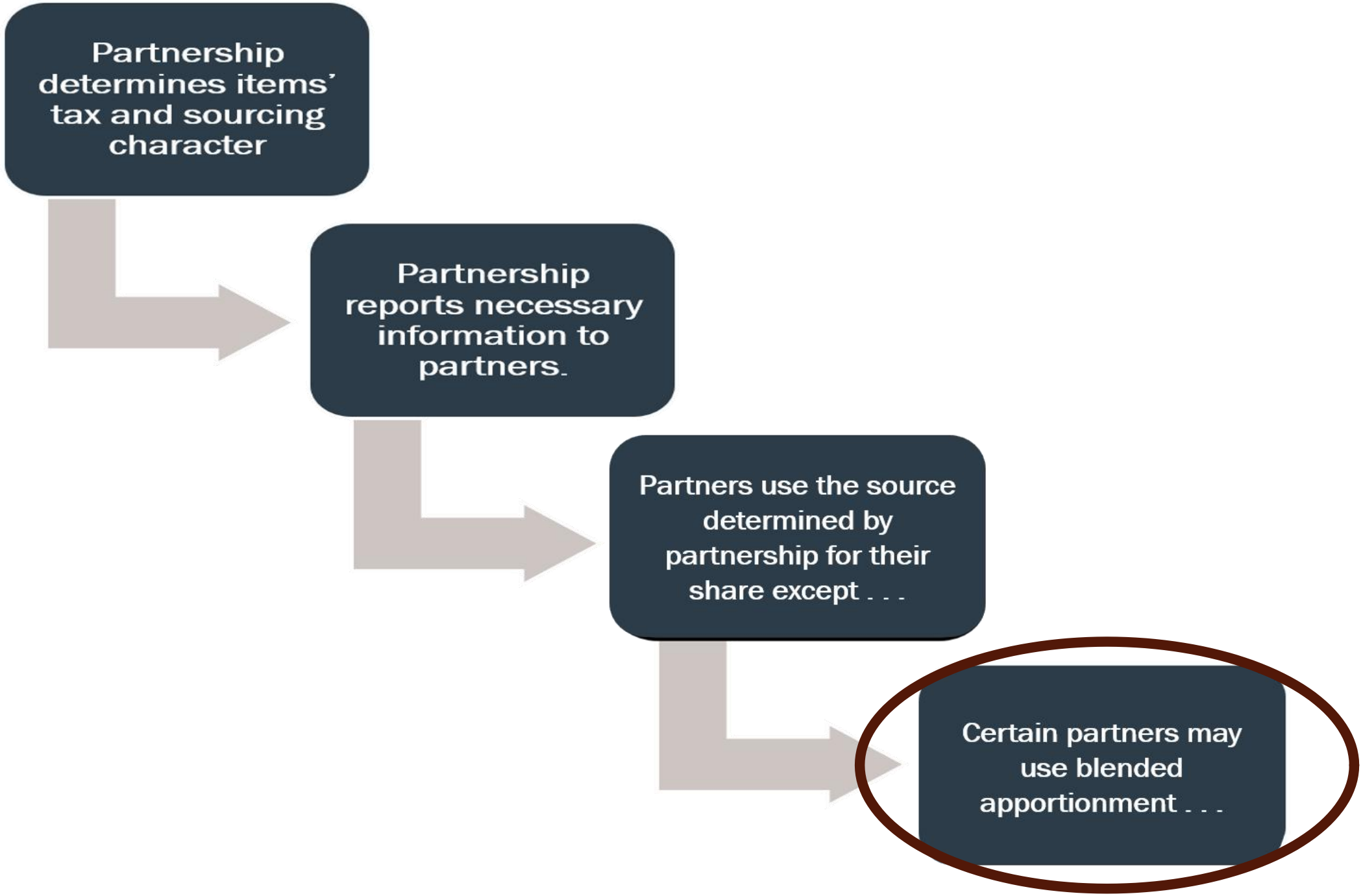
SOURCING PARTNERSHIP INCOME AND ITEMS – PART IV – (CONT'D)

(3) Information necessary for sourcing all non-apportionable items determined under Paragraph 2 under [REFERENCE TO STATE'S SOURCING RULES—TREATMENT OF NON-APPORTIONABLE OR NONBUSINESS ITEMS FOR CORPORATIONS OR NONRESIDENTS].

(4) Information on the apportionable income of the partnership as determined under [REFERENCE TO STATE'S SOURCING RULES—TREATMENT OF APPORTIONABLE OR BUSINESS ITEMS FOR CORPORATIONS OR NONRESIDENTS] based on the particular business activities to which the items making up that net apportionable income have a sufficient unitary relationship, including business activity conducted by one or more entities in which the partnership holds a direct or indirect interest, with the understanding that a partnership may engage in more than one unitary business. Guaranteed payments to partners for services are presumed to be part of the partnership's apportionable income.

SOURCING PARTNERSHIP INCOME AND ITEMS – PART IV – (CONT'D)

(5) Information on the partnership's apportionment factor attributes related to the items determined to be part of net apportionable income under Paragraph 4, applying [REFERENCE TO STATE'S SOURCING RULES—APPORTIONMENT FACTORS] to enable determination of those apportionment factors.


Partnership determines items' tax and sourcing character
Partnership reports necessary information to partners.
Partners use the source determined by partnership for their share except . . .
Certain partners may use blended apportionment . . .

TIERED AND CORPORATE PARTNERS & BLENDING

- The majority of states have rules that would use blended apportionment in some cases.
- Of the states that specify – most use distributive share as the basis for determining the partner's share of partnership apportionment factors.
- The MTC's combined filing model statutes (Joyce and Finnigan) also use blended apportionment and base the share of factors on the partner's distributive share.

THIS HAS LONG BEEN THE MODEL MTC RULE

MTC Joyce Model – adopted originally in 2006 –

"The [property, payroll, and sales] of a partnership shall be included in the determination of the partner's apportionment percentage in proportion to a ratio the numerator of which is the amount of the partner's distributive share of partnership's unitary income included in the income of the combined group in accordance with Section 3.C.ii.(c). and the denominator of which is the amount of the partnership's total unitary income.

WHY USE DISTRIBUTIVE SHARE?

- There are different possible methods for determining the share (or ratio) of factors when blending –
  - Specific assignment of factors based on items allocated to partners
  - Use of partner's capital to determine share
  - Use of distributive share

SPECIFIC ASSIGNMENT IS NOT POSSIBLE

- Problem – Partners may receive special allocations of certain expenses which have no clear connection to any apportionment factors used by the state and do not have a clear location of assignment (e.g. certain overhead expenses, interest expense, etc.).

USE OF CAPITAL MAY NOT REFLECT INCOME

- Problem – A partner may have very little capital but be allocated most of the income or vice versa. So, capital will not necessarily reflect income.

PROBLEM WITH DISTRIBUTIVE SHARE

- Partnerships do not necessarily allocate their items of income to partners using one proportionate ratio.
- Rather, different items may be allocated differently for various reasons—including "special allocations," mandatory or remedial allocations, and guaranteed payments (which have the same effect).

PROBLEM WITH DISTRIBUTIVE SHARE

- Simple example –
  - Partnership has $200 receipts and $160 expenses for a net of $40.
  - Partners A and B have equal capital
  - They agree to allocate to 80% of receipts to A and to 80% of expenses to B.
  - A's distributive share ratio is net $128/$40 = 320%
  - B's distributive share ratio is net ($88)/$40 = (220%)

WHY USE THE ABSOLUTE VALUE METHOD?

- Apportionment is not just about sourcing "positive" inputs to income, it's also about sourcing "negative" inputs.
- Assume a simple (if extreme) example:
  - Corporation has a unitary business with $10,000 of receipts in State A and $100,000 of expenses related to services provided by an independent contractor in State B, for a net loss of $999,000.
  - That loss—including ALL of the EXPENSES—are apportioned using the same apportionment factors that would be used if there was net income.

WHY USE THE ABSOLUTE VALUE APPROACH?

- Same simple example – with absolute value
  - Partnership has $200 receipts and $160 expenses for a net of $40.
  - Partners A and B have equal capital
  - They agree to allocate to 80% of receipts to A and to 80% of expenses to B.
  - A's distributive share ratio is ABS $192/$360 = 53%
  - B's distributive share ratio is ABS $168/$360 = 47%

WHY THE ABSOLUTE VALUE APPROACH?

- Computing absolute value is not hard.
  - Excel has always had this function as part of its spreadsheet – ABS ( )
  - It can be modified to fit the situation – so that the detail at which the method is applied fits the particular partnership's allocations of items.
- It's only needed for "disproportional" allocations. (So, if two 50/50 partners agree to split all items 80/20—the result is the same whether or not the ABS approach is used.

ONE LAST ALTERNATIVE

- Allowing taxpayers to simply use any “other reasonable methods” as they see fit.
- While writing that into a model statute is totally unworkable, there may be cases where the tax agency could approve the use of an alternative method and may want to explicitly reference that authority.

REMEMBER

- Blending is only used in when there is a "sufficient unitary relationship."
- Presumably, in those circumstances, the partner will have information about the partnership and will be able to obtain necessary information for applying the absolute value approach.

WHAT IS BLENDED APPORTIONMENT

	Partnership	Partner
Net apportionable income	$100,000	$100,000
Partner's distributive share	$50,000	
Receipts – State A	$200,000	$200,000
Receipts – Everywhere	$1,000,000	$400,000

No Blending

Partner's total income sourced to state A

$\frac{\$200,000}{\$400,000}$ X $100,000 = $50,000

+ $\frac{\$200,000}{\$1,000,000}$ X $50,000 = $10,000

Equals $60,000

Blending

Partner's total income sourced to state A

$100,000 + $50,000 = $150,000

X $\frac{50\% \text{ of } \$200,000 + \$200,000}{50\% \text{ of } \$1,000,000 + \$400,000}$ = 33.3%

Equals $50,000

SOURCING – PART IV – SECTION C
AS REVISED

(C) Upper-Tier Partnership and Other Pass-Through Entity Treatment of Items Allocated from Lower-Tier Partnerships:

Guaranteed payments and items of income, expense, gain, loss or other tax items that are allocated to an upper-tier partnership or other pass-through entity by a lower-tier partnership retain their tax character as determined in Subpart B regardless of whether the allocations are made in accordance with the partner's partnership interest, or are special, mandatory, or remedial allocations. But the upper-tier partnership or other pass-through entity will also determine the following with respect to these guaranteed payments and allocated items when reporting information to that upper-tier partnership's partners or the entity's beneficial interest holders:

SOURCING – PART IV – SECTION C (CONT'D)

1. Whether guaranteed payments or items determined by the lower-tier partnership to be non-apportionable under Subpart B.2, or apportionable under Subpart B.4, have a sufficient unitary relationship to any business activity generating apportionable income in which the upper-tier partnership or other pass-through entity is engaged directly or in conjunction with any entity in which the partnership owns a direct or indirect interest.

SOURCING – PART IV – SECTION C (CONT'D)

2. If any guaranteed payments or items determined to be non-apportionable by the lower-tier partnership are properly determined by the upper-tier partnership or other pass-through entity to have a sufficient unitary relationship to that partnership's or entity's own business activity generating apportionable income, then the upper-tier partnership or other pass-through entity will include these guaranteed payments and items in the apportionable income from that partnership's or entity's related business activities to be apportioned using the upper-tier partnership's or other pass-through entity's apportionment factors.

SOURCING – PART IV – SECTION C (CONT'D)

3. If any guaranteed payments or items determined to be apportionable by the lower-tier partnership are properly determined to have a sufficient unitary relationship to the upper-tier partnership's or other pass-through entity's business activity generating apportionable income, the upper-tier partnership or other pass-through entity will include these guaranteed payments and items in the apportionable income from that partnership's or entity's related business activity.

SOURCING – PART IV – SECTION C (CONT'D)

3. (cont'd) When sourcing this unitary apportionable income, the upper-tier partnership or other pass-through entity will include a share of the lower-tier partnership's apportionment factors from the related unitary business activity in the upper-tier partnership's or other pass-through entity's apportionment factors, aggregating the factor components. This inclusion of a share of lower-tier partnership factors with the partner's own factors will be referred to as the blending of apportionment factors. Under this calculation, the partner adds its share of the lower-tier partnership's factor components to its own factor components, and the partner's apportionment factors are recalculated based on the resulting aggregations.

SOURCING – PART IV – SECTION C (CONT'D)

4. The share of the lower-tier partnership's apportionment factors to be included when blending apportionment factors under Paragraph 3 of this subpart is determined using a ratio which is the partner's total unitary guaranteed payments and distributive shares of items computed using the absolute value of those items, divided by the total of all the unitary guaranteed payments and distributive shares of items to all partners of the lower-tier partnership computed using the absolute value of those items.

In determining the blended receipts factor, any receipts representing transactions between the partner and partnership will be eliminated from that blended factor to the extent of the partner's distributive share of the partnership items (receipts or expenses) associated with those transactions.

SOURCING – PART IV – SECTION C (CONT'D)

5. If any guaranteed payments or items allocated to the upper-tier partnership or other pass-through entity by the lower-tier partnership are properly determined not to have a sufficient unitary relationship to the upper-tier partnership's or other pass-through entity's business activity generating apportionable income, the upper-tier partnership or other pass-through entity will source these guaranteed payments or items as stated in the information from the lower-tier partnership as provided by Subpart B.

6. Upper-tier partnerships and other pass-through entities must provide sufficient sourcing information for their partners or beneficial interest holders to properly source their guaranteed payments or distributive share income in accordance with these provisions.

Note that the rules for corporate partners (in Sec. D) are similar when describing the approach to blending.

PART V APPLICATION OF FEDERAL TAX REQUIREMENTS, LIMITATIONS, AND ANTI-ABUSE RULES

- These provisions make clear how federal tax rules, including anti-abuse rules, apply in the state tax context.
- This is especially important where there is an impact on the state tax result, including the sourcing result, where there would be no effect on federal tax.

PART VI SUFFICIENT UNITARY RELATIONSHIP

- The application of the unitary business principle to partnership distributive share has not been addressed by U.S. Supreme Court.
- Partnerships serve different purposes – including conducting operations but also holding assets or serving as investments where the income would be part of the partner's unitary business.

SUFFICIENT UNITARY RELATIONSHIP – PART VI

A. The relationship between the partnership that recognizes the income or items and the partners . . . that are engaged in the related business activities generating other income or items, including:

1. The extent of actual common control, direct or indirect, held or exercised over the business activities, regardless of the share of partnership capital held;

2. The extent to which related activities are integrated or coordinated;

3. The extent to which resources and costs are shared; and

4. The extent of transactions or flows of value between the entities.

B. The extent of common use . . . of assets held by the partnership or partners.

C. The nature of common use . . ...

DISCUSSION

NEXT STEPS

PROCESS FOR APPROVING THE MODEL

- Work group presents the model to the Uniformity Committee for its consideration.
- The Uniformity Committee can take any action – approve the model with or without changes, send the model back to the work group, etc.
- If the Uniformity Committee approves the model – it goes to the MTC Executive Committee which can take any action, including holding a public hearing on the model.
- After the public hearing, the Executive Committee may review the hearing report and take any action.
- If the Executive Committee approves the model for consideration by the Commission, it will first hold a Bylaw 7 Survey of Compact and Sovereignty states.
- If the majority of states say they would consider the model, then it would be added to the agenda for the Commission's consideration.