



MULTISTATE TAX COMMISSION

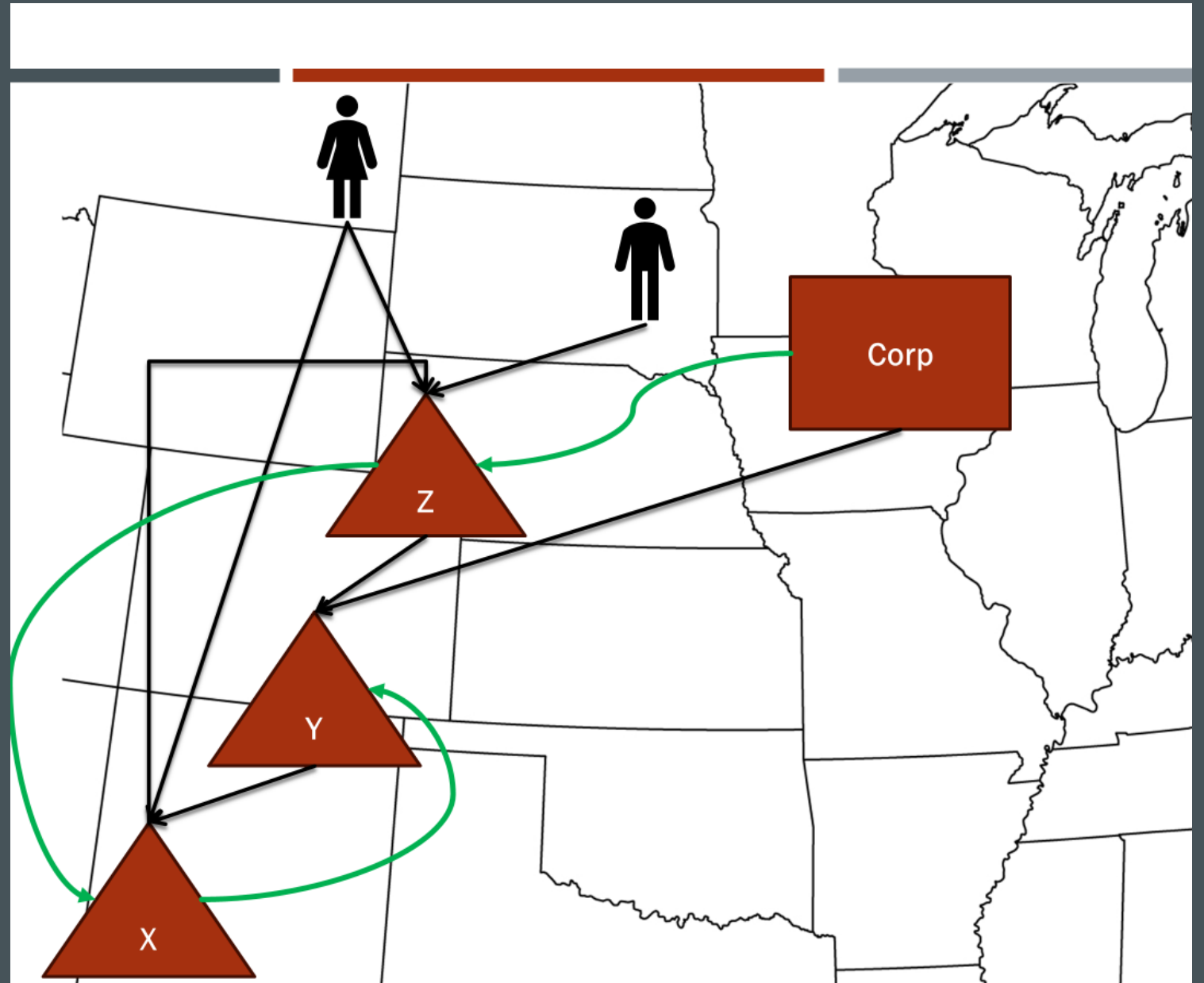
State Taxation of Partnerships – Status Report

SEPTEMBER 17, 2025

NOTE:

This presentation sets out information from the work group's discussions, white paper draft, and multistate research, which are on the project webpage here: [partnership project webpage](#). This information is presented to the work group for consideration and discussion. All input is welcomed.

**Our multistate research should not be relied on as tax advice. For specific questions, please contact your state department of revenue and/or tax advisor.*



Project Webpage

Click On

1. Uniformity
2. Uniformity Projects
3. State Taxation of Partnerships

The screenshot shows a web browser window with the URL `mtc.gov/uniformity/project-on-state-taxation-of-partnerships/`. The page features the MTC logo (Multistate Tax Commission) and a mission statement: "An intergovernmental state tax agency whose mission is to promote uniform and consistent tax policy and administration among the states, assist taxpayers in achieving compliance with existing tax laws, and advocate for state and local sovereignty in the development of tax policy." A search bar is located in the top right corner. A dark blue navigation bar contains the following menu items: "The Commission", "Uniformity", "Nexus", "Audit", "Events & Training", and "Resources". The main content area is titled "State Taxation of Partnerships" and includes a "Project Description" section. An arrow points from the "Uniformity" menu item to the "State Taxation of Partnerships" title.

mtc.gov/uniformity/project-on-state-taxation-of-partnerships/

MTC
MULTISTATE TAX COMMISSION

An intergovernmental state tax agency whose mission is to promote uniform and consistent tax policy and administration among the states, assist taxpayers in achieving compliance with existing tax laws, and advocate for state and local sovereignty in the development of tax policy.

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The Commission ▾ Uniformity ▾ Nexus ▾ Audit ▾ Events & Training ▾ Resources ▾

State Taxation of Partnerships

Project Description

At its meeting in April 2021, the Uniformity Committee took up a project on state taxation of partnerships based on the recommendations of the Standing Subcommittee that a work group be established to consider issues affecting:

- Sourcing of partnership operating income and partnership items for state tax purposes;
- Sourcing and taxation of gains and losses from the sale of partnership interests;
- Entity level taxation issues including transfer pricing or combined filing issues; and
- Other administrative and enforcement issues including information reporting and withholding.

On this project page and the links below, you will find:

- Information about upcoming and past meetings
- Project materials including whitepaper outline drafts
- Written comments and feedback
- Additional background information

PROJECT STATUS UPDATE

Recommendations for review

Anticipation of work group decision on whether to draft model rules

Anticipation of “aligning” these rules with the special rules for investment partnerships

RECOMMENDATIONS:

1. Use **terms** consistently with partnership law and Subchapter K and define other important terms to avoid ambiguity.

(See subsection I.B., C. and D.)

USING TERMS CONSISTENTLY

May require a process—

- Identifying common terms
- Noting usage
- Looking for questions or ambiguity
- Addressing by:
 - Amending – using different terms
 - Noting the particular use of the term in the context

RECOMMENDATIONS:

2. Recognize how the **attribution principle** may affect application of state tax rules.

(See subsection I.F.)

ATTRIBUTION PRINCIPLE

- Tax rules “stand alone” – they are not dependent upon the entity or aggregate theory.
- Character of income tax items depends on activity or assets.
- Attributes of partners are separate.
- Both may determine ultimate tax result.
- Subchapter K requires that the character of the income be determined at the partnership level and attributed to the partners.

RECOMMENDATIONS:

3. Adopt the following sourcing **framework** for sourcing partnership income (See subsection II.A.) :

- a. The **partnership will make a determination** of whether the items of income that it recognizes directly from its own activities are **apportionable income or non-apportionable income**, using information reasonably available.

RECOMMENDATIONS:

3. Adopt the following sourcing **framework** for sourcing partnership income (See subsection II.A.) :

- b. For items which the partnership determines to be **non-apportionable**, it will then **apply state rules of assignment** to determine the source of those items, based on their character, and will report this information to partners for their use.

RECOMMENDATIONS:

3. Adopt the following sourcing framework for sourcing partnership income (See subsection II.A.) :

- c. Partnerships will also determine their apportionment factors by state and will provide information sufficient for partners to use those factors in sourcing their share of the apportionable income directly recognized by that partnership.

RECOMMENDATIONS:

3. Adopt the following sourcing framework for sourcing partnership income (See subsection II.A.) :

- d. Partners will source their share of items determined by the partnership to be non-apportionable income based on the sourcing information provided by the partnership.

RECOMMENDATIONS:

3. Adopt the following sourcing framework for sourcing partnership income (See subsection II.A.) :

- e. Partners will source their share of items determined by the partnership (or the partner) to be apportionable income either by:
 - i. Applying the partnership's apportionment factors to those items, or
 - ii. Using blended apportionment.

RECOMMENDATIONS:

4. Use **absolute value of distributive share** for determining the share of partnership factors to include in the partner's apportionment factor when blending.

(See subsection II.B.)

ABSOLUTE VALUE OF DISTRIBUTIVE SHARE

- Capital ownership – doesn't necessarily represent partners' shares of income or items.
- Partner's "interest in the partnership" – is a term used in IRC 704(b) and also may not represent the partners' shares of income or items.
- Separate item receipts – won't work where there is a special allocation of expenses.
- Distributive share represents shares of items of partners, but special allocations may cause a partner's ratio to have a negative numerator and positive denominator, or vice versa.

RECOMMENDATIONS:

5. Apply blended apportionment when there is a sufficient unitary relationship between apportionable income of the partnership and apportionable income of the partner (detailed in subsection II. B.).

(See subsection II.B.)

RECOMMENDATIONS:

6. Consider a special rule for sourcing mandatory allocations of built-in gains or losses attributed to the contributing partner—at least in some situations.

(See subsection II.C.)

7. Consider how related-entity transactions not eliminated by blended apportionment may affect the sourcing of income and adopt special rules—including add-back statutes and transfer-pricing authority.

(See subsection II.D.)

RECOMMENDATIONS:

8. States may also need **anti-abuse rules**, similar to those adopted by the federal government, to prevent abusive income shifting.

- IRC § 7701(o) - general economic substance rules,
- IRC § 482 – transfer-pricing rules (see No. 7 above),
- IRS Reg. § 1.701-2 – general partnership anti-abuse rules,
- IRC § 704(b) – requirement for allocations to have substantial economic effect,
- IRC § 6222 – requirement for partner/partnership reporting consistency, and
- Rules for applying equitable apportionment when necessary.
(See subsection II.E.)

RECOMMENDATIONS:

9. When adopting more detailed rules, states should also consider limitations or exceptions that may simplify the application of state sourcing requirements to partnership income where there is little chance of abuse and where this would reduce compliance burdens.

10. Many states will also need to adopt more detailed partnership information reporting rules and forms to ensure partners have necessary information to source their distributive share.



QUESTIONS ON RECOMMENDATIONS?



ANTICIPATION OF DRAFTING MODEL RULES

- Project so far has gone step by step to ensure we're generally headed in the right direction.
- It appears that there is general consensus.
- But the devil is in the details.

ANTICIPATION OF DRAFTING MODEL RULES

- Assuming that there is consensus about the recommendations and the framework for the general approach, we can begin drafting models.
 - Models can serve as a “proof of concept.”
 - They can also highlight areas where a lack of uniformity can lead to multiple taxation, nowhere taxation, or undue complexity.

ANTICIPATION OF DRAFTING MODEL RULES

- **A similar exercise went on with the states in the 1950's, 60's and 70's**
 - **First states drafted and adopted UDITPA,**
 - **Then they drafted model rules for implementing UDITPA,**
 - **Over time, those rules have been updated and modified, adding more details and making changes as state policies evolved.**

ANTICIPATION OF DRAFTING MODEL RULES

- If there can be general consensus of the work group, considering any public comments, prior to the November uniformity committee meeting, we can ask the committee if they have any input.
- If there is agreement, we can proceed to begin drafting model rules.

“ALIGNING” WITH SPECIAL RULES FOR QIPS

- The special rules for qualified investment partnerships were drafted to apply a “look-through” approach in certain circumstances.
- The rules may not address fully how non-qualifying partners (active partners and corporate partners) will source their income.
- The rules may also not address how administrative expenses of the investment partnership are sourced.



QUESTIONS ON NEXT STEPS?

