



State Taxation of Partnerships – Status Report

MARCH 18, 2026

APPROACH

- **Research existing state rules**
- **Studying particular sourcing issues that may need to be addressed – to provide greater clarity or uniformity**
- **Drafting white papers on these issues**
- **Drafting model provisions**

KEEP IN MIND

- The provisions address **how state sourcing rules apply** to partnership income.
- Some unique partnership issues may call for uniform sourcing rules.
- **Consistency in sourcing with entity level taxes** is also key.
- Tax treatment –including sourcing—depends on the character of items.

KEEP IN MIND

- Partnerships determine the character of partnership items.
- The character of partnership items is attributed to the partners' shares.
- Attribution applies for state tax purposes, including when sourcing items.
- Tax attributes of the partner have a limited effect on sourcing.
 - Blending
 - Rare cases – non-apportionable items

KEEP IN MIND

- Application of the unitary business principle to partnerships is unclear.
- Anti-abuse rules and limits are essential.
- **Additional regulations will be needed** to implement the provisions here.
- As with partnership taxation generally, information reporting is essential.

COMBINED DRAFT MODEL PROVISIONS

- Sourcing where there are **Tiered and Corporate Partners**
 - Rule:
 - Character of items is determined at the partnership level—including any information relevant to whether the income is apportionable or non-apportionable
 - Character of items determines sourcing except where the partner's own tax attributes affect how the rules apply – especially where the partner has income from the same unitary business activities as the partnership
 - Blended apportionment using the **absolute value method**
 - Anti-abuse rules for other related-entity and pass-through issues affecting state sourcing

COMBINED DRAFT MODEL PROVISIONS

- Sourcing where there are **Tiered and Corporate Partners**
 - Scope:
 - Applying existing sourcing rules to distributive share income
 - General rules or sourcing approaches would presumably apply to all tax-paying partners
 - Specific rules are applicable to tiered and corporate partners

COMBINED DRAFT MODEL PROVISIONS

- Sourcing where there are **Tiered and Corporate Partners**
 - Effect:
 - Provides both essential general rules as well as specific rules for more complex partnership structures

COMBINED DRAFT MODEL PROVISIONS

- Sourcing Nonresident Partners' **Guaranteed Payments for Services**
 - Rule:
 - Sourced the same as the distributive share income
 - Also provides residents a credit for taxes paid to states taxing the payments based on performance of the services

COMBINED DRAFT MODEL PROVISIONS

- **Sourcing Nonresident Partners' Guaranteed Payments for Services**
 - **Scope:**
 - Guaranteed payments under IRC 707(c)
 - **Payments made for services, not capital**

COMBINED DRAFT MODEL PROVISIONS

- Sourcing Nonresident Partners' **Guaranteed Payments for Services**
 - Effect:
 - Consistent with the sourcing of distributive share

COMBINED DRAFT MODEL PROVISIONS

- Sourcing Income of **Investment Partnerships**
 - Rule:
 - The activities of the investment partnership in the state do not affect sourcing.
 - **Partners source income as if they held the investment assets directly** – using the state’s rules for sourcing income of partners taxed as nonresidents.

COMBINED DRAFT MODEL PROVISIONS

- **Sourcing Income of Investment Partnerships**
 - **Scope:**
 - **Partners –**
 - Taxed as nonresident individuals
 - Not actively involved in managing the investment activities
 - **Investment partnerships –**
 - As generally defined
 - With a safe harbor provision
 - Broader than the typical state definition of a qualified investment partnership

COMBINED DRAFT MODEL PROVISIONS

- Sourcing Income of Investment Partnerships
 - Effect:
 - An **exception to the general rule** for sourcing income of partnerships
 - Does not change the sourcing of income of corporate or tiered partners
 - Does not change the sourcing of income of managing partners



QUESTIONS

