Just Passing Through

An Update on the State Tax Treatment of Pass-Through Entities and Their Owners

ABA Tax Section SALT Committee
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Panel

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Agenda

- State Conformity to the Tax Cuts and Jobs Act of 2017 ("TCJA")
- Notable State Tax Developments Affecting Pass-through Entities
- Update on State Responses to the New Federal Partnership Audit/Assessment Rules
State Conformity to the Tax Cuts and Job Act of 2017 ("TCJA")
• IRS statistics continue to show that pass-through entities ("PTEs") are the favored form of business entity through 2017 (compared to 2016 returns)
  • C-Corporation Returns (Forms 1120) **declined by 7.1%**
  • S-Corporation Returns (Forms 1120S) **increased by 0.2%**
  • Partnership returns (Forms 1065) **increased by 1.0%**

• TCJA could reverse trends in entity form preference
  • Corporate rate reduced by 40% (from 35% to 21%)
    • Highest corporate rate (21%) significantly below highest individual rate (37%)
    • Offset by PTE tax deduction for certain pass-through entity owners (IRC §199A)?
  • Elimination of corporate alternative minimum tax
State Responses to SALT Deduction Limitation under TCJA

- States' reactions to SALT deduction limitation imposed by TCJA
  - States suing federal government
    - New York, joined by New Jersey, Connecticut and Maryland, sued Trump Administration for violating Due Process and 10th Amendment (State sovereignty)
  - Shifting personal income tax to employer payroll tax
    - New York's Employer Compensation Expense Tax (ECET)
      - Believed that few employers opted in for 2019
  - Creating of government sponsored charities
    - Contributions to charity result in tax credit against state and local liabilities (New York, New Jersey, Connecticut)
  - Pass-through entity level tax
State Responses to SALT Deduction Limitation under TCJA

- **Pass-Through Entity Tax Challenges**
  
  - Will the IRS respect the state pass-through entity tax structure?
  
  - Is a PTE paying a tax that an individual gets a personal income tax credit for the equivalent of the PTE paying the individual’s personal income tax liability?
    
    - See IRS Prop. Regs. 1.170A-1 aimed at shutting down the so-called government sponsored charities SALT deduction workarounds (hearing on Nov. 5, 2018)(final regulations now under review by OMB)
      
      - Invoke "quid pro quo" principles to deny the charitable deduction
      - Could it apply to a PE tax for which the individual taxpayer receives a corresponding state/local property tax credit?
      - Complex differences among IRC §§162, 164 and 170
• Pass-Through Entity Tax Challenges Cont.
  • For a nonresident PTE owner, will their resident state provide an "other state tax credit" (OSTC) for their share of the PTE tax paid to the other state?
    • Connecticut's pass-through entity tax regime builds in an OSTC
    • NJ already provides an OSTC for its residents for NYC UBT
    • CA FTB denies OSTC through a letter ruling
  • Nonresident PTE owners cannot offset income earned at the entity level by personal deductions or losses from other PTE business activities in determining nonresident tax
  • In some variations, the PTE tax is NOT elective
    • If it is elective, does that minimize its validity in a challenge by the IRS under the SALT deduction limitation?
    • Veto messages by CA and MI Governors
State Responses to SALT Deduction Limitation under TCJA

- Connecticut enacted Public Act 18-49 5/31/18, effective 1/1/18
  - 6.99% entity-level income tax on most PTEs in Connecticut (mandatory)
  - Owners' credit against their CT personal income tax for 93.01% of their distributive or pro rata share of the PTE-level tax paid
  - CT Guidance on estimated payments (SN 2018(4), 6/6/18), the calculation (OCG-6, 6/19/18), and the owner credit (OCG-7, 8/21/18)

- Wisconsin enacted Public Act 368
  - Created an optional tax on pass-through entities with an offsetting exclusion for entity members
State Responses to SALT Deduction Limitation under TCJA

- Other states considering it
  - Michigan – SB 1170 (passed the Legislature – vetoed by the Governor)
  - New York – Discussion draft for unincorporated Business Tax (May 2018)
    - (Not in FY 2020 Budget)
  - Arkansas – draft bill before Tax Reform and Relief Legislative Task Force
  - Minnesota – SF 304 was introduced January 22, would allow pass-throughs to elect to be treated as C Corporations and pay a flat tax at the entity level.
  - Louisiana – SB 223 was introduced April 10, would allow pass-throughs to elect to be subject to the corporate income tax.
CT Pass-Through Entity Tax
- Effective for tax years starting on or after 1/1/18
- Imposed on Partnerships, LLCs, S corporations
  - Does not apply to PTPs, C corporations or SMLLCs
- Entity Level Income Tax Rate: 6.99%
- Entity and Partner Level Impact
  - Pass-through entity can deduct the tax for federal income tax purposes
  - Partners' receive less ordinary income, paying less federal income tax
- Pass-through owner is entitled to a credit equal to 93.01% of his/its direct or indirect share of the pass-through entity's tax liability provided the pass-through entity has paid such liability prior to the owner claiming the credit
  - Credit may be used by owner against Connecticut Corporation or Income Tax
  - Credit is refundable for individuals and may be carried forward for corporations
• **CT Pass-Through Entity Tax (cont.) - Two Methods For Calculating Taxable Income**
  - Standard/Default
    - All of pass-through entity's Connecticut source income is subject to tax – regardless of partner type
  - Alternative Base (Elective Method - Annual)
    - Only income attributable to owners who are individuals (including any owner subject to the personal income tax) is subject to tax
    - Income attributable to corporations, 501(c)(3) organizations, insurance companies is not included in pass-through entity tax calculation
  - Potential issues raised
    - Tax is not imposed on guaranteed payments
      - The Connecticut portion of guaranteed payments is determined by multiplying guaranteed payments by the pass-through entity's apportionment factor
      - Requires nonresident individuals who receive guaranteed payments to file an individual state return
  - Nonresident owners may end up paying more tax in their state of residence
    - Other states may not allow a credit for the Connecticut pass-through entity tax
      - Entity level tax not imposed on individual
      - Owner already received a credit for it against Connecticut Income Tax
      - Tax exempt entities share of Connecticut pass-through tax
State Responses to SALT Deduction Limitation under TCJA

**New York State Draft Unincorporated Business Tax Law**
- New York Dept. of Tax. & Fin. issued a proposed discussion draft of a new unincorporated business tax (UBT) which would be effective January 1, 2019 (May 2018)
  - Would provide an offset credit at the partner level against NYS individual income tax
- Unincorporated business net income would be the sum of:
  - Federal ordinary business income (under IRC Section 702(a)(8)) as applied to the partnership under IRC Section 702;
  - Taxes paid or incurred during the taxable year under this new UBT by the affected partnership to the extent deducted in computing federal ordinary income; and
  - Guaranteed payments paid by the affected partnership to its partners under IRC Section 707(c).
  - Provides instructions for reporting Section 965 inclusion and corresponding deduction for PTEs and their owners:
    • If NYS return already filed, PTE must file an amended return
    • If NYS return NOT filed, PTE must use these instructions
  - A NYS taxpayer must use amounts reported on its federal IRC 965 Transition Tax Statement and the Statement MUST be attached to the NYS return
    • The notice also provides guidance for trusts and fiduciaries
• Partnerships
  • NYS Partnership return (IT-204-I)
    • Do not make any NYS modifications to IRC Section 965 amounts
  • NYS Partner K-1 (IT-204-IP) for Article 22 Partners
    • Include IRC Section 965(a) on the federal "other income" line (Line 11) and IRC Section 965(c) on the federal "other deductions" line (Line 13)
    • NYS amounts reported on reciprocal lines only "... to the extent that the stock of a corporation generating the IRC Section 965 income was used in a trade or business in New York"
  • NYS Corporate Partner K-1 (IT-204-CP) for Article 9-A Partners
    • Same guidance as above for federal "other income" and "other deduction" lines (Lines 54 and 56, respectively)
    • No guidance on apportionment
IRC §199A - 20% deduction for PTE owners

- IRC §199A Deduction for Qualified Business Income (TCJA §11011)
  - 20% individual owner deduction for income received from PTEs
  - PTE includes sole proprietorship, partnerships, S corporations and LLCs
  - Dividends received from cooperatives, real estate investment trusts (REITs) and publicly traded partnerships (PTPs) also qualify
  - Intended to provide an equalized federal rate reduction for PTE owners compared to owners of a C-corporation
    - 20% deduction (for 37% taxpayer) = 29.6% federal tax rate
State Conformity to IRC §199A

• Even among rolling conformity states, most states won’t automatically follow IRC §199A due to another provision of the TCJA most likely not intended by Congress
  • Congress wanted the PTE deduction to be in addition to the standard deduction
  • TCJA §11011(b) sets forth how the 20% PTE deduction is applied for federal income tax purposes:
    • Subsec. 1 - Not deductible under IRC §62(a) - Defines “Adjusted Gross Income” (AGI)
    • Subsec. 2 - Deductible under IRC §63(b) - Defines “Taxable Income” (TI)
  • Allowing deduction against TI (instead of AGI) allows non-itemizers to claim deduction
State Conformity to IRC §199A

- According to the Federation of Tax Administrators*:
  - Most states use AGI as the starting point for determining their state personal income tax base
  - Only six states use TI

<table>
<thead>
<tr>
<th>Colorado</th>
<th>Minnesota</th>
<th>Oregon</th>
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<tr>
<td>Idaho</td>
<td>North Dakota</td>
<td>South Carolina</td>
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- Minnesota, Oregon, and South Carolina have indicated they will not conform
- Idaho has indicated they will allow the deduction – nothing formal released
- Colorado and North Dakota have not indicated whether they will allow or not
- Except for these six, unless the state legislature expressly chooses to conform, the IRC §199A deduction will not apply for state tax purposes
  - Expect a state “addback”
  - Iowa and Washington D.C. have affirmatively conformed

- Federal limitation on excess business interest expense applied at partnership level, so it may increase partnership's income for purposes of:
  - Entity level taxes
  - Nonresident withholding
  - Composite returns
  - New Jersey issued guidance indicating the partnership can use 100% of the interest expense and 163(j) will not apply at the partnership level.
- Carryforward of excess business interest expense applied at the partner level which may create issues for state taxes, especially nonresident partner withholding and composite tax returns.
- Nonresident carryforward rules and tracking of state sourced disallowed interest expense.
  - Currently, state administrative rules do not exist in most states
  - Rules may be similar to Passive Loss Rules and NOL rules
  - Cost of compliance vs. impact on credit for taxes paid to other states
- Electing out of Composite Returns, in the year of the 163(j) limitation and in the year the Excess Business Interest is carried forward to.
  - Does the state tax savings justify the compliance cost?
  - How certain is the tax savings?
• **California** - State Tax News (July 2018)
  • TCJA repealed the partnership technical termination provisions (IRC §708(b)(1)(B))
    • Under prior IRC, a 50% or more change in the ownership of a partnership within a 12-month period required the partnership to “terminate”
    • Most (ABA Tax Section, AICPA, even IRS) agreed this rule was unnecessary
  • Franchise Tax Board does not conform to repealed provision
    • California is fixed date conformity state (IRC as of January 1, 2015)
    • Partnership could have one federal year but two California short-years (two annual taxes and potentially two LLC fees for LLCs)
  • Real Estate Transfer Tax considerations in light of *926 N. Ardmore LLC*
Notable State Tax Developments Affecting Pass-through Entities

  - Permits taxpayers to join in a class action to recover overpaid LLC fees that were unapportioned
  - Trial court denied class certification to force the FTB to pay the refunds
  - Appellate court reverses and finds "this matter [is] eminently suitable for treatment on a classwide basis."
    - California Supreme Court denied further review of class treatment on October 31, 2018 — class action can move forward
  - *Bunzl?*
California Nexus Considerations

- Arizona v. California, Case No. 22O150 (U.S. S.Ct.)
  - Motion for leave to file a Bill of Complaint with the U.S. Supreme Court, filed on February 28, 2019
    - U.S. Supreme Court would have original jurisdiction
    - Special Master would be appointed; case could take years
  - Arizona is challenging California’s extraterritorial assessment and collection of its $800 “doing business” tax imposed on LLCs and corporations, including out-of-state companies that have no connection to California except for a passive investment in a California company
  - Arizona asserts California’s actions violate the Due Process and Commerce Clauses
    - Arizona argues California’s extraterritorial assessments “impressively manage” to violate all four prongs of Complete Auto
    - California’s extraterritorial seizures from taxpayers’ banks violate Due Process
  - Does Arizona have standing to sue California?
    - Arizona asserts five different cognizable injuries
**Idaho** - *(I/M/O [redacted]), Idaho State Tax Comm., Dkt. o-976-965-632 (Nov. 8, 2017)*

- Tax Commission finds gain on the sale of partnership interest to be business income and subject to standard apportionment.
- Uses alternative apportionment to modify the property and sales factors to include 12% historic average apportionment to Idaho of the FMV of goodwill and gross proceeds in property and payroll factor, respectively.
  - Department would have had a 40.5% factor v. taxpayer 13.7% factor
  - Tax Commission alternative is 13.5% factor
• **Illinois** – HB 4798 (Welch) Proposal to Increase Personal Property Replacement Tax Rate
  - Would increase rates from 1.5% to 7.5% for partnership, LLC, S-Corp and trust partners
  - The corporate replacement tax rate (2.5%) would remain unchanged.
  - Exemption for investment partnerships would be eliminated from the replacement tax
Minnesota


- Distinguishing 2010 ruling in HMN Financial, 782 N.W. 2d 558 (MN S. Ct. 2010)
- Court upheld the use of alternative apportionment for a bank’s attempt to treat two LLCs disregarded for federal income tax purposes as non-“financial institutions” and apply the bank’s financial institution apportionment method to the LLCs.

Financial institutions – include loan interest in sales factor

Non-financial institutions do not include loan interest
Montana - Mont. Admin. R. 42.9.112 and 42.9.303; amended
Mont. Admin. R. 42.9.107 and 42.15.120

- Provides income apportionment and allocation rules for PTEs
- Under the rule, partnerships that are unitary with the business
operations of a corporate partner and whose apportionment factors are
included in the computation of that corporate partner's apportionment
factors are considered to be part of the corporate group for purposes of
applying the Finnigan rule.
New Jersey Developments
Withholding and Nexus

  - Tax Court grants summary judgment to limited partnership precluding NJ Div. of Tax. from assessing withholding tax on corporate partner's income wherein partnership received timely withholding exemption form from corporate partner
  - Corporate partner sought to revoke its withholding exemption form by filing amended returns in response to *BIS LP, Inc. v. Div. of Tax.*, 26 N.J. Tax 489 (App. Div. 2011) that its activities in NJ were not enough to create nexus
  - Issue of nexus and tax to be determined at corporate partner level

• A NYC ALJ held that a corporation with no NYC business activities was subject to tax in NYC on the gain from its sale of a minority interest in an LLC that was doing business in NYC.
  - Petitioner owned a passive minority interest in the LLC, which was taxed as a partnership for federal income tax and NYC purposes, and Petitioner was not engaged in the conduct of a unitary business with the LLC.
  - The ALJ determined that the City could impose its GCT on the gain from the sale of the Petitioner’s interest in the LLC because the LLC appreciated in value and enjoyed the protection, opportunities and benefits that the City conferred on it and "the City provided the LLC with a successful environment, which resulted in LLC's appreciation in value, and this created the City's right to receive something in return."
  - The ALJ determined that the imposition of GCT on the capital gain did not violate the Due Process Clause or Commerce Clause of the United States Constitution.

- NJ resident S-corporation owners entitled to OSTC only to the extent income was apportioned to PA using PA tax rate but NJ’s apportionment rules and income computation method
- Taxpayer can’t claim credit for full amount of tax paid to PA

<table>
<thead>
<tr>
<th>2012 Return information</th>
<th>New Jersey (OSTC)</th>
<th>Pennsylvania (Actual Tax Paid)</th>
</tr>
</thead>
<tbody>
<tr>
<td>S-corporation Income</td>
<td>$2,108,894</td>
<td>$2,252,820</td>
</tr>
<tr>
<td>PA apportionment (NJ 70% sales, PA Single Sales Factor)</td>
<td>69.5464%</td>
<td>81.7087%</td>
</tr>
<tr>
<td>PA apportioned income</td>
<td>$1,466,660</td>
<td>$1,840,750</td>
</tr>
<tr>
<td>PA tax rate (NJ top rate 8.97%)</td>
<td>3.07%</td>
<td>3.07%</td>
</tr>
<tr>
<td>Tax</td>
<td>$45,026</td>
<td>$56,511</td>
</tr>
</tbody>
</table>
• **New York** - *Nonresident Partner’s Treatment of Gain or Loss on Certain Sales or Transfers of a Partnership or Membership Interest*, TSB-M-18(2)I (April 6, 2018)

  • If a nonresident is a partner in a partnership where a sale or transfer of the interest of the partner is subject to IRC §1060, any gain recognized for federal income tax purposes from the transaction is treated as New York source income allocated based upon the New York Business Allocation Percentage (BAP) during the year of the sale or transfer. No minimum ownership threshold.

  • Effective for transactions on or after April 10, 2017.
Ohio - IT-2016-01 (reissued Dec. 1, 2017)
  - Updated guidance on sourcing of gain on nonresident's sale of partnership interest

State law provides (O.R.C. §5747.212) that if a nonresident individual partner/owner owns more than 20% then must apportion gain on sale of partnership interest to Ohio.

- OH Supreme Court found O.R.C. §5747.212 unconstitutional under the Due Process Clause in Corrigan v. Testa, 2016-Ohio-2805
  - Dept. states that Corrigan only found the statute unconstitutional "as applied" to that taxpayer and declined to find the statute unconstitutional on its face
  - Provides instructions on how affected taxpayers can pursue refund claims
**North Carolina**


- N.C. S.Ct. affirms lower court rulings that state could not impose personal income tax on trust whose only contact with the state was the North Carolina residence of its beneficiaries. *Cf.* LLC and its members?
  - Court finds the trust did not have "sufficient minimum contacts" with NC under the Due Process Clauses of the federal and North Carolina Constitutions.
    - Trust was established in and governed by the law of New York in 1992 for benefit of children of the settlor
    - Trustee replaced and new trustee was a Connecticut resident
• **N.C.G.S. §105-160.2** ..."The tax is computed on the amount of the taxable income of the estate or trust that is for the benefit of a resident of this State, ..."
  
  • Trust claimed that the statute was unconstitutional on its face and as applied to the plaintiff under Due Process and Commerce Clauses of the U.S. Constitution and under the Due Process Clause of the North Carolina Constitution
  
  • Court chooses only to address the constitutional issue under an "as applied" to the taxpayer standard (does NOT strike down the statute as to all taxpayers.)
    
    • Finds no “purposeful availment” of North Carolina by the Trust
      
      • Cites to *Quill* ... (remember this is before June 21, 2018 decision in *Wayfair*)
      
      • However, N.C. court is ONLY looking to *Quill*’s “minimum contacts” analysis.
      
      • Trust is treated as an entity separate and apart from its beneficiaries.
      
      • Mere contact with a North Carolina resident beneficiary is not enough.

• U.S. Supreme Court grants cert.: oral argument was held in April
• Minnesota


• Minn. S.Ct. affirms Minn. Tax Court rulings that statutory definition of "resident trust" violated the Due Process Clauses of the Minnesota and the U.S. Constitutions as applied to the trusts.
  
  • Court finds the trusts lack sufficient relevant contacts with MN to be permissibly taxed, consistent with due process, on all sources of income as residents.
  
  • Similar to the N.C. S.Ct. ruling in *Kaestner 1992 Trust*

• Petition for cert. filed with U.S. Supreme Court
• **Tennessee Single Sales Factor For Asset Managers**
  - SB 2256 enacted April 9, 2018 provides a single sales factor apportionment election for 'Financial Asset Management Companies' doing business in Tennessee
    - Applies to both excise and franchise taxes
    - Election must be made with an originally filed return
    - Effective for a minimum of five years.
  - Report of TN General Assembly Fiscal Review Committee stated that no financial asset management companies were located in Tennessee at the time of enactment and the legislation is intended to promote such companies to move to the state.
  - Alliance Bernstein announced it was moving 1,000 jobs to Nashville from New York
• *Unpublished Decision - Cook v. Oregon Department of Revenue; August 8, 2017, TC 5298*

  • Taxpayer is a nonresident of Oregon who held ownership interests in several passthrough entities (PTEs) some of which engaged in business in Oregon
  • Taxpayer calculated Oregon income by adding Oregon income from PTEs that operated in Oregon
  • Taxpayer excluded income from PTEs that did not have Oregon operations
  • Oregon DOR argued that Taxpayer needed to include his distributive share of all PTEs in taxable income and calculate an Oregon apportionment factor to apply to his distributive share
    • Would create a quasi combined filing at the individual level
  • Oregon Tax Court ruled in favor of Taxpayer
  • Apportionment is calculated at the PTEs level and then individual nonresident partner reports his pro-rata share of Oregon income from each of the PTEs with Oregon source income
Updates on State Responses to the New Centralized Federal Partnership Audit/Assessment Rules
• The Bipartisan Budget Act of 2015 Adopted New IRS Audit Procedures for Partnerships and Multi-Member LLCs
  • HR 1314 (P.L. 114-74) enacted in 2015
  • Projected $9.3 Billion revenue-raiser (federal alone)
    • Consolidated Appropriations Act of 2018, HR 1625 (P.L. 115-141), enacted in March 2018, made several useful technical corrections and added a unique new “pull-in procedure” described later in these slides

• The New Audit Rules For Taxable Years Beginning After December 31, 2017
  • Option to elect into the new rules for earlier years (few did so)

• Expected to raise additional tax revenue by enabling the IRS to more efficiently audit “large” partnerships and LLCs
  • According to Government Accountability Office (GAO), less than one percent of large partnerships were audited during 2012, compared to a 27 percent audit rate of corporations with assets exceeding $100 million
State Issues
Presented
Under Federal
Centralized
Partnership
Audit Regime
• **Issues the states need to address:**
  • State procedural rules need to be amended to match the new federal partnership audit and adjustment process
    • Whether to allow different treatment at the state level
    • How to treat amended federal returns taxpayers may file during the modification period
    • How are partnerships that pay the tax subject to state reporting requirements
  • Can partnerships simply file amended returns (entity returns along with any composite or withholding returns) and K-1s for partners and have partners file amended returns for the reviewed year?
  • Proper allocation and apportionment of federal adjustments
  • How to collect tax owed when the liability will have accrued years earlier and the partnership may be defunct or partners may have moved from the state or from U.S.
State Effects – Apportionment

- At the federal level, the IRS can impose tax on 100 percent of any adjustment. For state purposes, that adjustment often needs to be apportioned and/or allocated if the partnership is operating or doing business in multiple states.
  - Many states use different apportionment rules for partnerships that are part of a unitary business
- If the partnership pays, the payment is being made on behalf of its partners.
  - Can the partnership’s apportionment factor be used as a general rule?
  - How do resident individual partners calculate their credits for taxes paid to other states?
    - Will other states provide credit to partners for tax paid by the partnership in another state?
  - Can a partnership seeking to pay the tax on behalf of its direct and indirect partners be forced to know (and certify?) the residency status of its indirect partners?
State Effects – Nexus Considerations

- At the federal level, the IRS has jurisdiction to collect tax from all partnerships and partners. States, however, may only impose and collect tax on taxpayers with the requisite contacts and substantial nexus (pesky Constitution!).
  - Should/can the new audit rules expand the state's ability to impose and collect tax from out-of-state partners?
  - Nexus can vary year by year – partnership activity in state can change along with partners' residency status in a state

- **Example:** Nevada partnership with five partners—four are California individual residents and one is a Nevada individual.
  - Original Return Filing: The partnership does not file a California return because it does not do business in the State. California partners report 100 percent of their partnership income on their California individual returns.
• MTC "Partnership Project" work group referred model to Uniformity Committee -
  • Website: [http://www.mtc.gov/Uniformity/Project-Teams/Partnership-Informational-Project](http://www.mtc.gov/Uniformity/Project-Teams/Partnership-Informational-Project)
  • July 24, 2018, MTC Uniformity Committee approved and referred model to MTC Executive Committee
  • October 15, 2018 public hearing held on the model act
  • October 26, 2018, Hearing Officer Report issued
  • November 8, 2018, MTC Executive Committee tentatively OK’d –
New Federal Partnership Audit Rules: State Implications

- **State Legislative Activity to Date**
  - 2016—only Arizona passed a bill
    - Arizona bill does not comprehensively address federal changes (e.g., fails to address tiered partnerships)
  - 2017—five states proposed legislation but all died/failed
  - 2018—California, Georgia and Hawaii enacted conformity legislation; Minnesota introduced legislation but bill died
    - Hawaii’s legislation is problematic because it merely incorporates by reference certain IRC audit procedure provisions
  - 2019 —
    - West Virginia passed legislation
    - Minnesota and Oregon introduced legislation
    - California FTB introduced tech corrections bill
    - Hawaii
## Comparison of Federal Process to Draft State Model

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<thead>
<tr>
<th>Federal Audit Reporting Process</th>
<th>Draft MTC State Model Process</th>
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<tbody>
<tr>
<td>Default – Partnership pays the tax using highest individual/corporate income tax rates</td>
<td>Default – Partnership notifies partners and partners pay the tax (composite/withholding filers still subject to partnership paying the tax)</td>
</tr>
<tr>
<td>Has option for partners to file amended returns (or simply pay (&quot;pull-in&quot;) to remit tax</td>
<td>Such partners required to report under the general reporting requirements at the state level (i.e., file separate amended state return). Those partners are not be included in any partnership pays tax calculation.</td>
</tr>
<tr>
<td>Has option for partnership to &quot;push-out&quot; tax to review year partners to remit the tax when they file their tax return for the year IRS completes the audit (adjustment year)</td>
<td>“Push-out” option requires reporting and payment on an amended return for original (&quot;reviewed&quot;) year. Ability to report/pay tax on current year tax return unavailable (likely an administrative systems issue w/most states)</td>
</tr>
<tr>
<td>Tiered Partners – must complete all filings by the extended due date of the Audited Partnership's return for the adjustment year</td>
<td>Subject to extension, Tiered Partners must complete all reporting and payments 90 days after the extended due date of the Audited Partnership's return for the adjustment year</td>
</tr>
<tr>
<td>Federal Audit Reporting Process</td>
<td>Arizona SB 1288 (2016)</td>
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<td>-----------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Default – Partnership pays the tax using highest individual/corporate income tax rates</td>
<td>Follows federal, but partnership is required to file an amended return for the reviewed year</td>
</tr>
<tr>
<td>Has option for partners to file amended returns (or simply pay (&quot;pull-in&quot;)] to remit tax</td>
<td>Not addressed in SB 1288; unclear whether covered by general reporting provisions</td>
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<tr>
<td>Has option for partnership to &quot;push-out&quot; tax to review year partners to remit the tax when they file their tax return for the year IRS completes the audit (adjustment year)</td>
<td>If partnership &quot;pushed-out&quot; at the federal level, partners will be required to report and pay any additional tax on an amended return for original (&quot;reviewed&quot;) year. Ability to report/pay tax on current year tax return unavailable (likely an administrative systems issue w/ mos: states)</td>
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<td>Tiered Partners – must complete all filings by the extended due date of the Audited Partnership's return for the adjustment year</td>
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Questions?
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