

Following is model statutory language that can be used to implement a State tax on partnerships and S corporations. Also included in the language set forth below are provisions to be included in the relevant State personal income tax and corporate income tax statutes, with such provisions allowing for a complete offset of any unincorporated business entity tax liability against the personal income tax liability of the direct and indirect individual members of the pass-through entity by means of a credit. If the member cannot use the credit in any year, the credit will carryforward to future years, with no expiration. In addition, a credit is provided against the personal income tax liability for residents to the extent that a similar pass-through entity tax is imposed on the resident's share of income sourced to the other state.

The language reflected below provides that pass-through entities will be able to elect to be subject to this Partnership level tax, with any such election needing to be made on an annual basis.

Model Pass-Through Entity Tax

1 Section 1. (NEW) *(Effective from passage and applicable to taxable years*
2 *commencing on or after January 1, 2018)* (a) As used in this section and
3 section 2 of this act:

4 (1) "Partnership" has the same meaning as provided in Section
5 7701(a)(2) of the Internal Revenue Code, and any regulations adopted
6 thereunder. "Partnership" includes a limited liability company that is
7 treated as a partnership for federal income tax purposes;

8 (2) "S corporation" means a corporation or limited liability company that is
9 treated as an S corporation for federal income tax purposes;

10 (3) "Taxable year" means the taxable year of a partnership or S
11 corporation for federal income tax purposes;

12 (4) "Affected business entity" means any partnership or S corporation
13 that elects to be subject to tax pursuant to Section 2 of this Act;

14 (5) "Member" means (A) a shareholder of an S corporation, (B) a
15 partner in (i) a general partnership, (ii) a limited partnership, or (iii) a
16 limited liability partnership, and (C) a member of a limited liability
17 company that is treated as a partnership or S corporation for federal

18 income tax purposes;

19 (6) "Direct member" means a member that holds an interest directly in
20 an affected business entity; and

21 (7) "Indirect member" means a member that itself holds an interest,
22 through a direct or indirect member that is a partnership or an S
23 corporation, in an affected business entity.

24 (b) (1) Each affected business entity that is a partnership and that
25 is **[each State shall insert its doing business language]** in this state
26 shall, on or before the **[each State shall insert its required filing date]**
27 following the close of each taxable year, pay a tax
28 in an amount equal to (A) (i) the separately and nonseparately computed
29 items, as described in Section 702(a) of the Internal Revenue Code,
30 of the affected business entity, to the extent derived from or connected
31 with sources within this state, as determined under the provisions of **[citation**
32 **to the relevant section of the State personal income tax statute]**, (ii) as decreased
33 by the deduction allowed under Section 199A of the Internal Revenue Code
34 computed as if such deduction was allowed to be taken by the affected
35 business entity for federal tax purposes **[subdivision (B) should be**
36 **included in the statutory language in those States that allow individual**
37 **members to take the 199A deduction in determining their State personal**
38 **income tax liabilities]**, and (iii) as increased or decreased by any modification
39 described in section **[citation to any desired modification provisions in State**
40 **statute]** that relates to an item of the affected business entity's income, gain, loss or
41 deduction, to the extent derived from or connected with sources within this state,
42 as determined under the provisions of **[citation to the State personal income**
43 **tax]**, (B) multiplied by **[relevant tax rate to be imposed on affected business**
44 **entities]**. If the amount calculated under subdivision (A) of this subsection
45 results in a net loss, such net loss may be carried forward to succeeding
46 taxable years for which the affected business entity elects to be
47 subject to tax pursuant to section 2 of this Act until fully used. Payment
48 shall be made with the return that is required to be filed under section **[citation**
to any State statute requiring the filing of composite returns].

49 (2) Each affected business entity that is an S corporation and that is **[each State**
50 **shall insert its doing business language]** in this State, shall, on or before the
51 **[each State shall insert its required filing date]**
52 following the close of each taxable year, pay a tax in an amount equal to
53 (A) (i) the separately and nonseparately computed items, as described in Section
54 1366 of the Internal Revenue Code, of the affected business entity, to the extent
55 derived from or connected with sources within this state, as determined under the
56 provisions of **[citation to the relevant section of the personal income tax statute]**,

57 (ii) as decreased by the deduction allowed under Section 199A of the Internal
58 Revenue Code computed as if such deduction was allowed to be taken by
59 the affected business entity for federal tax purposes, **[subdivision (B)**
60 **should be included in the statutory language in those States that allow**
61 **individual members to take the 199A deduction in determining their State**
62 **personal income tax liabilities]** and (iii) as increased or decreased by any
63 modification described in section **[citation to any desired modification provisions**
64 **in State statute]**, as amended by this act, that relates to an item of the affected
65 business entity's income, gain, loss or deduction, to the extent derived from or
66 connected with sources within this state, as determined under the provisions of
67 **[add reference to the cite for the State personal income tax]**, (B) multiplied by
68 **[relevant tax rate to be imposed on affected business entities]**. If the amount
69 calculated under subdivision (A) of this subsection results in a net loss, such net
70 loss may be carried forward to succeeding taxable years for which the
71 affected business entity elects to be subject to tax pursuant to section 2 of this
72 Act until fully used. Payment shall be made with the return that is required to
73 be filed under section **[citation to any State statute requiring the filing of**
74 **composite returns]**.

75 (c) If an affected business entity is a direct or indirect member of another affected
76 business entity, the member affected business entity shall, when calculating
77 its net income or loss pursuant to subdivision (b)(1)(A) or (b)(2)(A) of this section
78 1 of this act , subtract its distributive share
79 of income or add its distributive share of loss from the affected business entity in
80 which it is a direct or indirect member to the extent that the income or loss was
81 derived from or connected with sources within this state.

82 (d) A nonresident individual who is a member shall not be required
83 to file an income tax return under the provisions of **[add reference to the cite**
84 **for the State personal income tax]** for a taxable year if, for such taxable year,
85 the only source of income derived from or connected with sources within the
86 state for such member, or the member and the member's spouse if a joint
87 federal income tax return is or shall be filed, is from one or more affected
88 business entities and such affected business entity or entities file and pay the
89 tax due under this section.

90 (e) Each partnership and S corporation shall report to each of its members,
91 for each taxable year, such member's direct pro rata share of the tax
92 imposed under this section on such partnership or S corporation if it is an
93 affected business entity and its indirect pro rata share of the tax imposed on any
94 affected business entity in which such affected business entity is a direct or indirect
95 member.

96 (f) (1) (A) Each person that is subject to the tax under **[add cite to the State’s**
97 **personal income tax]** and is a member shall be entitled to a credit against
98 the tax imposed under said **[add cite to the state’s personal income tax]**. Such
99 credit shall be in an amount equal to such person's direct and indirect pro rata
100 share of the tax paid under this section by any affected business entity of
101 which such person is directly or indirectly a member multiplied by **[insert a**
102 **potential haircut percentage on the credit equal to (100-(100-the tax imposed at**
103 **the entity level) to reflect that the income passed-through to the Member will**
104 **reflect the reduced tax and thus less of a credit may be needed at the entity level**
105 **to offset the Member’s personal income tax liability attributable to income from**
106 **the affected business entity]**. If the amount of the credit allowed
107 pursuant to this subdivision exceeds such person's tax liability for the tax
108 imposed under said chapter, such unused amount shall be carried forward to
109 each of the succeeding taxable years by the person until such credit is fully taken
110 against the tax under **[add cite to the state’s personal income tax]**.

111 (B) Each person that is subject to the tax under **[add reference to the cite for the**
112 **State personal income tax]** as a resident or a part-year resident of this state and is a
113 member shall be entitled to a credit against the tax imposed under said **[add cite to**
114 **the State’s personal income tax]** for such person's direct and indirect pro rata
115 share of taxes paid to another state of the United States or the District of Columbia,
116 on income of any partnership or S corporation of which such person is a member
117 that is derived therefrom, provided the taxes paid to another state of the United
118 States or the District of Columbia results from a tax that the **[State agency or**
119 **commissioner]** determines is substantially similar to the tax imposed under this
120 section. Any such credit shall be calculated in the manner prescribed by the **[State**
121 **agency or commissioner]**, which shall be consistent with the provisions of
122 section **[add cite to the State personal income tax credit provisions]**. If the amount
123 of the credit allowed pursuant to this subdivision exceeds such person's tax liability
124 for the tax imposed under said chapter, such unused amount shall be carried
125 forward to each of the succeeding taxable years by the person until such credit is
126 fully taken against the tax under **[add cite to the State’s personal income tax]**.

127 (2) Each company that is subject to the tax under **[add cite to the State’s corporate**
128 **income tax]** and is a member shall be entitled to a credit against the tax imposed
129 under said **[add cite to the state’s corporate income tax]**. Such credit shall be in an
130 amount equal to such company's direct and indirect pro rata share of the tax paid
131 under this section by any affected business entity of which such company is a
132 member multiplied by **[insert a potential haircut percentage equal to (100-(100-the**
133 **tax imposed at the entity level) to reflect that the income passed-through to the**
134 **Member will reflect the reduced tax and thus less of a credit may be needed at**
135 **the entity level to offset the Member’s corporate income tax liability attributable**
136 **to income from the affected business entity]**. Such credit shall be applied after all

137 other credits. Any credit that is not used in the taxable year during which the
138 company reports the net income from such affected business entities
139 shall be carried forward to each of the succeeding taxable years
140 by the company until such credit is fully taken against the tax under **[add cite to**
141 **the State's corporate income tax]**.

142 The provisions of sections **[citation to any desired administrative procedure**
143 **provisions in State statute, including any estimated payment provisions]** shall
144 apply to the provisions of this section in the same manner and with the same force
145 and effect as if the language of said sections had been incorporated in full into this
146 section and had expressly referred to the tax under this section, except to the
147 extent that any such provision is inconsistent with a provision of this section.

148 Sec. 2. (NEW) (*Effective from passage and applicable to taxable years commencing on*
149 *or after January 1, 2018*) (a) A partnership or an S corporation may elect in the
150 manner set forth in subsection (b) of this section to become an affected business
151 entity that is required to pay the tax under section 1 of this act in any taxable
152 year. A separate election shall be made for each taxable year.

153 (b) (1) An election under subsection (a) of this section shall be made on such
154 form and in such manner as the **[insert state agency or commissioner]** may
155 prescribe by regulation or instruction.

156 (2) An election under subsection (a) of this section may be made for any
157 taxable year at any time on or before the **[each state shall insert its required**
158 **election date]** of such taxable year.

159 (3) An election made under paragraph (b)(1) of this Section 2 of the act must
160 be signed by:

161 (A) Each member of the electing entity who is a Member at the time the
162 election is filed; or

163 (B) Any officer, manager, or Member of the electing entity who is
164 authorized (under local law or the entity's organizational documents)
165 to make the election and who represents to having such authorization under
166 penalties of perjury.