

ARIZONA DEPARTMENT OF REVENUE

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ARIZONA CORPORATE TAX RULING **CTR 93-4**

**(On November 23, 2012 certain references were updated, see the footnotes for details.
No substantive changes were made.)**

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

ISSUE:

What are the Arizona filing requirements for a partnership and its corporate partners that have elected exclusion from partnership treatment for federal tax purposes?

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 43-102 sets forth the legislative intent to adopt the provisions of the federal Internal Revenue Code relating to the measurement of taxable income for corporations, partnerships, estates and trusts subject only to the modifications in Title 43.

Internal Revenue Code (I.R.C.) § 761(a) provides for an exclusion from subchapter K of the Internal Revenue Code (Partners and Partnerships) for certain unincorporated organizations.

Treasury Regulation (Treas. Reg.) § 1.6031(a)-1(c)(ii)¹ provides the rule for excluding an unincorporated organization from filing additional federal partnership returns beyond the first year of elected exclusion.

Treas. Reg. § 1.761-2 provides rules for excluding an unincorporated organization from the application of the partner and partnership sections of the Internal Revenue Code.

¹ This Treasury Regulation reference was updated to reflect its new number on November 23, 2012. The regulation referenced when this ruling was issued was Treasury Regulation § 1.6031-1(b)(ii). No substantive changes were made.

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A.R.S. § 43-104² defines "taxpayer" as any person subject to a tax imposed by Title 43 and defines "person" to include individuals, fiduciaries, partnerships and corporations.

A.R.S. § 43-1401.2 defines "Arizona taxable income" of a partnership to mean its Arizona gross income adjusted by the modifications specified in A.R.S. §§ 43-1021 and 43-1022.

A.R.S. § 43-1412 requires, that in computing the taxable income of a partner, each partner must include its distributive share of the partnership's Arizona taxable income.

DISCUSSION:

I.R.C. § 761(a) provides that the members of an unincorporated organization, under certain circumstances, may elect to be excluded from the application of the provisions of all or part of Subchapter K (Partners and Partnerships) of the Internal Revenue Code.

The Arizona Department of Revenue will recognize and accept a valid federal election made pursuant to I.R.C. § 761(a) and Treas. Reg. § 1.761-2 if the electing organization meets all of the following requirements:

1. The electing organization files an Arizona Partnership Income Tax Return (Form 165) with page one completely filled out for the year the election is made.
2. The appropriate line on Form 165 is checked as being the partnership's final return with the notation "see attached federal election." Zero should be entered on lines one through six if there is no distributive income and no additions to or subtractions from distributive income.
3. A copy of the valid federal election (federal Form 1065 and statement) required by Treas. Reg. § 1.761-2 must be attached to the Arizona Form 165.

If in future years, after a valid election has been made, the organization is sent an Arizona Form 165 by the Department, the organization should send in the form and indicate on Line E (or its equivalent³) that a valid election has been made pursuant to I.R.C. § 761(a).

² When this ruling was issued this paragraph referred to Arizona Administrative Code rule R15-2-1132(A) for the definitions of "taxpayer" and "person". However, these definitions were removed from the rules because they repeated the definitions already contained in A.R.S. § 43-104. Therefore, on November 23, 2012 this reference in this paragraph was changed to A.R.S. § 43-104. No substantive changes were made.

³ Line E at the time that this ruling was issued asked about the filing of returns in the prior two years. The equivalent on the 2011 form was line I. This footnote was added on November 23, 2012.

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The corporate partner is required to file an Arizona corporate income tax return (Form 120) either apportioning or allocating its distributive share of the partnership's income or loss.

RULING:

The Arizona Department of Revenue will recognize and accept a valid federal election made pursuant to I.R.C. § 761(a) and Treas. Reg. § 1.761-2 if the three requirements above are met. The corporate partner of an electing partnership is required to report its distributive share of the partnership's income or loss.

Harold Scott, Acting Director

Signed: March 29, 1993

Explanatory Notice

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law which are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement which provides interpretation, details or supplementary information concerning the application of the law. **Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax ruling.** See GTP 92-1 for more detailed information regarding documents issued by the Department of Revenue.