**EXEMPT PUBLICLY TRADED PARTNERSHIPS FROM**

**LEGISLATION REQUIRING WITHHOLDING FOR NONRESIDENTS**

Publicly traded partnerships (“PTPs”), often known as master limited partnerships or MLPs, are partnerships which are traded on public exchanges. Shares in a PTP are known as “units.” A typical PTP has millions of units outstanding held by tens of thousands of individual investors. The unitholders of each PTP are scattered among the 50 states and the District of Columbia, and sometimes territories or foreign countries as well. While some smaller PTPs are limited to one or a few states, the majority are multistate businesses, and some operate in over 40 states.

PTPs should be exempted from any requirement that partnerships withhold state income tax from distributions to nonresident partners or otherwise pay tax on behalf of these partners because:

# A withholding regime is administratively burdensome for the PTP and accurate withholding is impossible. Because a PTP is publicly traded, thousands of units may change hands every day. Moreover, most of the units are held in street name by brokers, who report the information on unitholders only once a year, for the purpose of providing partnerships with the information needed to send K-1s out to their unitholders. Thus, the PTP has no way of knowing from whom it should withhold each quarter. In addition, because income tax is calculated based on income and loss for an entire year, and withholding is quarterly, the partnership has no real way of knowing at the time it must withhold what will be the amount of income (or loss) attributable to the state for which tax is being withheld.

* **The state would also face an administrative burden.** State revenue departments would find the burden of administering withholding to be highly disproportionate to the small amount revenue received. Revenue officials would be faced with processing hundreds of thousands of tax payments related to PTPs operating in their states and remitting refunds on many of them. Revenue departments in other states that have examined this possibility—most notably, New York--have concluded that they want no part of withholding from PTP distributions, and have communicated this to their legislatures.
* **Withholding from distributions is a mismatch of tax to income.**  An investor in a PTP is taxed not on the cash distribution he receives, but on his allocated share of the PTP’s income. This is true whether or not he receives a cash distribution. The cash distribution is treated as a return of capital and is not taxed. While a partnership’s income situation may affect the level of cash distributions, they are entirely different items and there is no direct correlation between them. It is thus inappropriate to withhold from one the tax owed on the other.
* **The taxable income for each partner, if any, is small.** By the time partnership income is divided among the states where it was earned, and then allocated among tens of thousands of partners, the amount of taxable income per partner is very small, often below the state’s personal exemption or standard deduction. Because of various tax benefits passed through to partners, it may even be negative. This has been borne out by analysis of partnership tax information by PricewaterhouseCoopers.
* **It would compromise** “fungibility” of PTP units. In order to be publicly traded, a security must be identical in all respects, including tax attributes, to all other securities in its class, so that it does not matter to an investor which particular unit he owns. If state tax is paid for nonresident but not other partners, units will have different tax attributes and fungibility is lost. Theoretically this could halt trading in a PTP’s units.
* **The Multistate Tax Commission** **recommends excluding PTPs from withholding**. After considering all these arguments, the Multistate Tax Commission included an exclusion for PTPs in its model legislation relating to withholding for nonresidents.
* **The majority of states have excluded PTPs from their withholding requirements.** These include California, Connecticut, Kentucky, Georgia, Louisiana, Massachusetts, Michigan, Nebraska, New Jersey, New York, North Dakota, Ohio, Oregon, Oklahoma, Pennsylvania, Utah, and more than a dozen others.