

**CHAPTER 107. PARTNERSHIPS AND ASSOCIATIONS**

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**§ 107.1. General taxability of partners and members.**

A partner or member of an association shall report his share of the net income of a partnership or association for its taxable year ending within or with the taxable year of the partner or member. The share of a partner of the net income of a partnership shall include his share of any guaranteed payments received from the partnership. The share of a partner of income shall be reported as net profits from the operation of a business, profession or other activity, net gains or income from disposition of property, net gains or income derived from or in the form of rents, royalties, patents and copyrights, dividends, interest, gambling or lottery winnings, or net gains or income derived through estates and trusts, depending upon which class it shall fall within.

**§ 107.2. Taxability of resident and nonresident partners and members.**

(a) The share of a partner or member of the net income of a partnership or association shall be his share of the net income whether or not distributed.

(b) A partner or member who is a resident of this Commonwealth shall report his entire share of the net income from the partnership or association regardless of where the income was earned.

(c) A partner or member who is a nonresident of this Commonwealth shall report only income of the partnership or association from sources within this Commonwealth.

**§ 107.3. Determination of income.**

Net income of a partnership or association shall be determined and reported on the basis of accepted accounting principles and practices after provision for all costs and expenses incurred in the conduct thereof. Deductions may not be allowed for expenses not related to the production of income, nor may taxes based on income be allowed as a deduction.

**Notes of Decisions***Constitutional*

Retirement contributions made on behalf of partners is money that the partners would otherwise receive in their share of the net profits of the partnership, and the contributions are made, at least theoretically, at the election of the partners. On the other hand, when an employer makes contribu-

tions to an employee's retirement plan, the contributions are not made by reducing the employee's salary, and the employee is given no control over whether the contributions are to be made. Furthermore, the employee does not actually or constructively receive the contributions because the receipt of benefits under the retirement plan could be subject to substantial limitations and restrictions. There is, therefore, a legitimate and nonarbitrary reason for distinguishing between partners and employees, thus rendering the Department of Revenue's regulations constitutional. *Smith v. Commonwealth*, 684 A.2d 647 (Pa. Cmwlth. 1996).

#### *Partnerships*

Because partners acquire the status of self-employed individuals, any contributions to a retirement plan are not expenses related to the production of income, and therefore, may not be deducted from the partnership's net profits. *Smith v. Commonwealth*, 684 A.2d 647 (Pa. Cmwlth. 1996).

### **§ 107.4. Formation of a partnership of association.**

The transfer of property or anything else of value to a partnership or association in exchange for an interest therein may give rise to income or gain subject to tax under § 103.13 (relating to net gains or income from disposition of property).

### **§ 107.5. Liquidation of a partnership or association.**

The transfer of cash or property to a partner or member of a partnership or association in liquidation of his interest therein shall give rise to gain or loss to the extent of the difference between the cash and fair market value of other property received and the base of the partner or member for his partnership or association interest immediately before the distribution.

### **§ 107.6. Tax returns.**

Partnerships and associations deriving income from sources within or occupying an office within this Commonwealth shall file a tax information return annually. Reference should be made to § 117.17 (relating to partnership returns).

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