This article summarizes the findings of a survey and accompanying report prepared by a joint task force consisting of members of the Committee on State and Local Taxation and the Partnerships and LLCs Committee of the ABA Section of Taxation. At issue is whether, and to what extent, state tax administrators plan to conform to the Federal classification of “Series LLCs,” once the proposed regulations are finalized. The task force solicited responses to its survey and prepared its final report, which is expected to be issued on Monday, May 6.

**Update: Will the States Conform to Federal Classification Of Series LLCs Once the Proposed Regulations Are Finalized?**

**By Bruce P. Ely, J. Leigh Griffith, and James E. Long, Jr.**

By way of background, on Sept. 14, 2010, the U.S. Department of Treasury and the Internal Revenue Service issued proposed income tax regulations dealing with “series” entities such as series limited liability companies (“Series LLCs”), series business or “statutory” trusts, and segregated portfolio companies (the “Proposed Regulations”). Generally, the Proposed Regulations classify each series within a Series LLC as a separate entity, which can then make the same tax elections as a regular LLC, e.g., to be classified as a partnership (if it has more than one member), to be disregarded (if it has only one member), or to be taxed as a C or S corporation. Under the Proposed Regulations, the Series LLC itself (as opposed to the series within the Series LLC) is considered a separate tax reporting unit independent of the various series within it, but is not required to file a Federal income tax return or information return unless it has its own income, deductions, or credits, independent of the series within it, in any given taxable year.

The Proposed Regulations govern only Federal income tax issues; they expressly reserve a determination as to the Federal (and state) employment tax issues. The Proposed Regulations requested comments from interested parties, and the IRS specifically requested comments from the ABA Section of Taxation. The task force developed the survey in response to the Treasury’s and IRS’s request for employment tax classification, but expanded the scope to include state income, net worth/gross receipts, and transactional taxes. Surveys were sent to the relevant departments or agencies for all 50 states, the District of Columbia, and Puerto Rico. Responses were received from the relevant departments or agencies of 31 states. Some of the responding state departments or agencies did not respond to all of the questions asked. A brief summary of the responses is provided below.
State Employment Taxes

The IRS and the Treasury Department specifically requested comments on “[h]ow series and series organizations will be treated for state employment tax purposes and other state employment-related purposes and how that treatment should affect the Federal employment tax treatment of series and series organizations (comments from the states would be particularly helpful).” Nine (9) states (Alabama, Florida, Kentucky, Massachusetts, Missouri, Nebraska, North Dakota, South Dakota, and Wisconsin) indicated that they would treat each series as a separate employer for state employment taxes, while five (5) states (Iowa, Minnesota, New Jersey, Nevada, and Oregon) said they would not treat each series separately. The remaining states were either undecided or we have not received a response from their agency responsible for state employment taxes.

Other State Taxes

Although the IRS’s and Treasury Department’s request for comments was limited to employment taxes, the Task Force determined that seeking input from the states regarding the classification of Series LLCs for other state tax purposes (especially income/net worth and transactional taxes) would be beneficial to taxpayers, tax administrators, and practitioners. With respect to income taxes, twenty-two (22) states so far have responded that they would follow the Proposed Regulations, once finalized, by classifying each series as a separate reporting entity that can make its own income tax election. Of the 31 states responding to the survey,2 no state indicated that it would not follow the Federal rules, once finalized, although six (6) states were undecided (Alabama, Hawaii, Indiana, Maryland, Minnesota, and Ohio). Although not responding to the survey, the Texas Comptroller’s Office has ruled publicly that, for purposes of its margin tax, Texas will not follow the Proposed Regulations but will instead treat all series as one taxpayer.

With respect to sales and use taxes, the states were more varied regarding whether to follow the Proposed Regulations, once finalized. Only thirteen (13) of twenty-eight (28) states indicated that they would follow the Federal rules for purposes of their sales and use taxes; ten (10) states were undecided; two (2) states responded that they would not follow the Federal rules for this purpose; three (3) states responded “not applicable;” and Texas’s response suggests that it would not follow the Federal rules based on its single entity position. Tennessee responded that it would exempt from sales and use taxation any transfers of tangible personal property between and among the series because, for state law purposes, there is no change of title or ownership. In a supplemental response, Virginia indicated it would also consider the Series LLC one entity for sales and use tax purposes, and thus, transfers between or among the series would not be subject to its sales or use tax.

The task force’s report has been delivered to Treasury and the IRS for initial review and comment. The final report will be discussed at the Tax Section’s Mid-Year Meeting on May 10.

The authors, who were principally responsible for soliciting responses to the survey and preparing the report, are deeply grateful to the many state departments of revenue and similar state agencies who took the time to respond thoughtfully to the joint task force’s questionnaire.

2 North Dakota did not respond to this question; South Dakota and Nevada both checked “Not Applicable.”