Minnesota Department of Revenue

Revenue Notice # 26-02: Estate, Fiduciary, S-Corporation Taxes – Apportionment of Income - Electing Small Business Trust

Introduction

This Revenue Notice addresses the apportionment of income for the S-portion of an Electing Small Business Trust (ESBT).

Background

With an ESBT, the trust is taxed in its capacity as a shareholder of an S-corporation pursuant to *Minnesota Statutes,* section 290.9726. The income character provisions set forth in *Internal Revenue Code,* section 1366(b), apply as if realized from the source or incurred in the same manner as the S-corporation. The department's position in determining the Minnesota taxable income of the S-portion of an ESBT starts with whether the S-portion of the trust has the requisite minimum contacts with the state pursuant to *Minnesota Statutes,* sections 290.014 and 290.015.

Once it is determined that the S-portion of the trust has the requisite minimum contacts with the state, the calculation of Minnesota taxable income starts with federal taxable income as defined in *Internal Revenue Code,* section 63, pursuant to *Minnesota Statutes,* section 290.01, subdivision 19. Minnesota modifications as set forth in *Minnesota Statutes,* sections 290.0131, 290.0132, and 290.0135, are added and subtracted from federal taxable income to arrive at net income before apportionment. Generally, net income before apportionment of the S-portion of an ESBT is business income.

Department's Position

Business income of the S-portion of the ESBT is apportioned pursuant to *Minnesota Statutes,* sections 290.17, 290.191, and 290.20. These same principles apply to tax preference items and the source to which it relates. The business income apportioned to the state combined with any nonbusiness income allocable to the state constitute Minnesota taxable income of the S-portion of the trust.

When a trust has income from both the S-portion of an ESBT and from other sources owned by the trust, that income is reported in the form and manner prescribed by the commissioner. The income is apportioned or allocated pursuant to *Minnesota Statutes,* sections 290.17, 290.191, and 290.20, following the position outlined above.

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