

# NAEA February 2024 Solutions Room

## Pass-Through Entity Tax (PTET)

Allan "A.J." Reynolds, EA



# NAEA February 2024 Solutions Room February 08, 2024

## Allan “A.J.” Reynolds, EA

- Immense experience in various areas of taxation, which encompasses over 30 years
- Practice centers on individual, business, & estate tax preparation
- Specializes in diverse areas of IRS Representation
- Iowa Legal Aid volunteer for Tax Court cases & other tax issues



## Quote of the Session

**“THE ONLY THING THAT HURTS MORE THAN  
PAYING AN INCOME TAX, IS NOT HAVING TO  
PAY AN INCOME TAX.”**

**-- Thomas Dewar --**

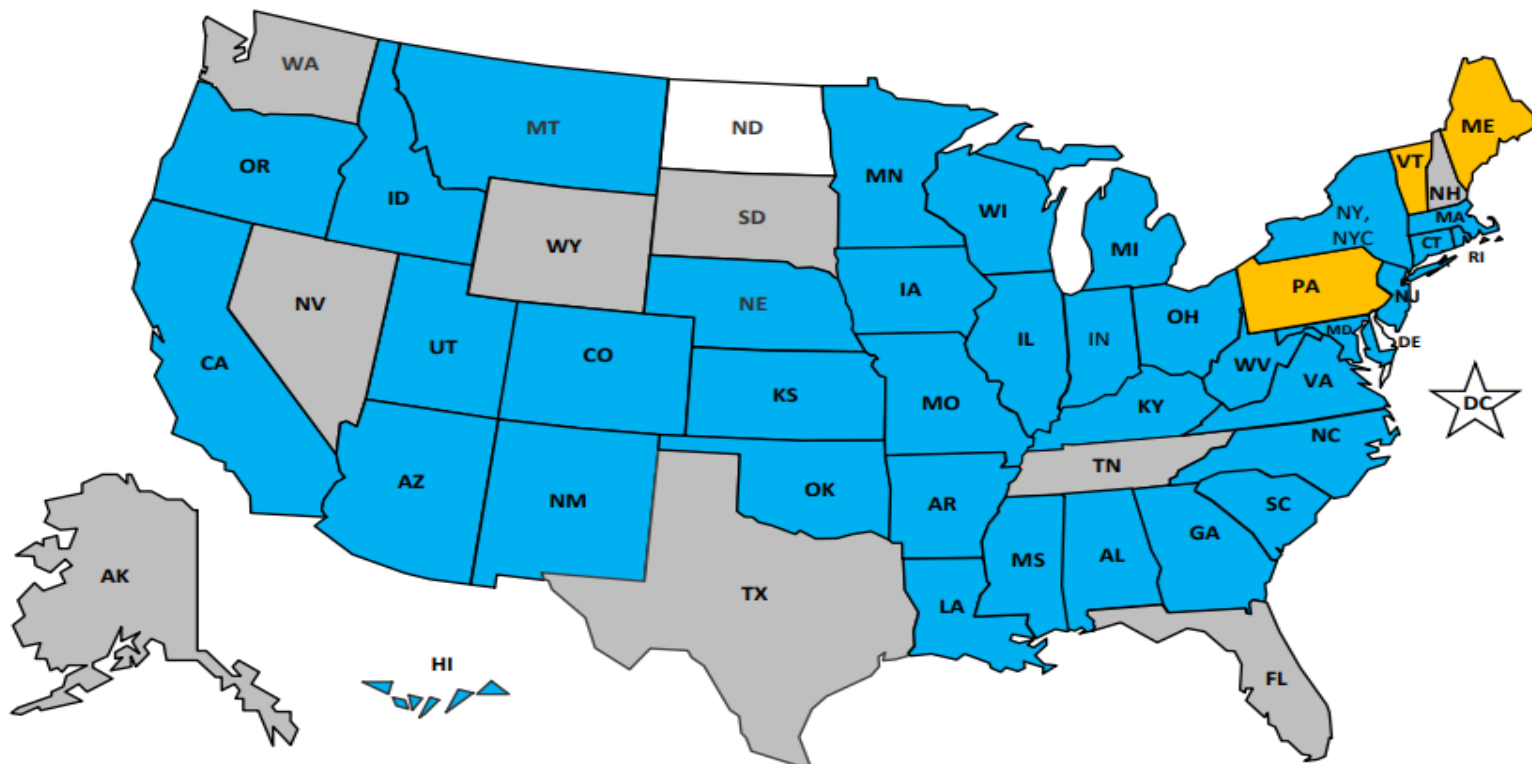
# February 2024 Solutions Room – PTET

**What is a Pass-Through  
Entity Tax (PTET)?**

# February 2024 Solutions Room – PTET

## States with Enacted or Proposed Pass-Through Entity (PTE) Level Tax

As of December 19, 2023



● 36 states (& 1 locality) that enacted a PTE tax since TCJA SALT deduction limitation, effective for 2021 (or earlier) unless noted:

[AL](#), [AR<sup>1</sup>](#), [AZ<sup>1</sup>](#), [CA](#), [CO<sup>3</sup>](#), [CT<sup>4</sup>](#), [HI<sup>2</sup>](#), [GA<sup>1</sup>](#), [IA<sup>1</sup>](#), [ID](#), [IL](#), [IN<sup>1</sup>](#), [KS<sup>1</sup>](#), [KY<sup>1</sup>](#) (& [KY](#)), [LA](#), [MA](#), [MI](#), [MD](#), [MN](#), [MO<sup>2</sup>](#), [MS<sup>2</sup>](#), [MT<sup>2</sup>](#), [NC<sup>1</sup>](#), [NE<sup>3</sup>](#), [NJ](#), [NM<sup>1</sup>](#), [NY](#), [OH<sup>1</sup>](#), [OK](#), [OR<sup>1</sup>](#), [RI](#), [SC](#), [UT<sup>1</sup>](#), [VA](#), [WI](#), [WV<sup>1</sup>](#), and [NYC<sup>1</sup>](#)

<sup>1</sup> Effective in 2022

<sup>2</sup> Effective in 2023 or later

<sup>3</sup> Retroactive to 2018

<sup>4</sup> Mandatory 2018-2023, elective starting 2024

● 3 states with proposed PTE tax bills:  
ME - [LD 1891](#) carried over to next session  
PA - [SB 659](#) referred to Finance; [HR 1584](#) referred to Finance

VT - [SB45](#) passed Senate, referred to House Ways & Means

● 9 states with no owner-level personal income tax on PTE income:  
AK, FL, NH, NV, SD, TN, TX, WA, WY

○ 3 states with an owner-level personal income tax on PTE income that have not yet proposed or enacted PTE taxes:  
DC, DE, and ND

<https://us.aicpa.org/advocacy/state/statetaxresources>



# February 2024 Solutions Room – PTET

## Current PTE tax workarounds (36 states and 1 locality)

State	Effective Year	State	Effective Year
Alabama	2021	Minnesota	2021
Arizona	2022	Mississippi	2022
Arkansas	2022	Missouri	2022
California	2021	Montana	2023
Colorado	2018 (retroactive)	Nebraska	2018 (retroactive)
Connecticut	2018 (mandatory 2018-2023, elective starting 2024)	New Jersey	2020
Georgia	2022	New Mexico	2022
Hawaii	2023	New York	2021
Idaho	2021	New York City	2022
Illinois	2021	North Carolina	2022
Indiana	2022 (retroactive)	Ohio	2022
Iowa	2022 (retroactive)	Oklahoma	2019
Kansas	2022	Oregon	2022
Kentucky	2022 (retroactive)	Rhode Island	2019
Louisiana	2019	South Carolina	2021
Maryland	2020	Utah	2022
Massachusetts	2021	Virginia	2021
Michigan	2021	West Virginia	2022
		Wisconsin	2018



<https://us.aicpa.org/advocacy/state/statetaxresources>

# Attendance Check #1

Please answer the poll in Zoom.  
If you are unable to enter your  
answer in the poll you can use  
the chat or Q&A box.



# February 2024 Solutions Room – PTET

## □ What is PTET and / or why to we have it?

✓ TCJA and \$10,000 SALT limitations

✓ IRS Notice 2020-75

❖ Main Guidance

✓ Workaround





# February 2024 Solutions Room – PTET

## □ What is PTET and / or why to we have it?

### ✓ Items that do not apply to SALT limitations

- ❖ Foreign taxes

- ❖ Taxes in § 164(a)(1) and (2) incurred with carrying on a trade or business

# February 2024 Solutions Room – PTET

## □ What are SITPs

- ✓ **Specified income tax payments**
- ✓ **IRS Notice 2020-75 defines as any amount paid by a PTE to satisfy its liability for income taxes defined under § 164(b)2 for which a deduction is not disallowed**
  - **SITP is an amount paid by a PTE to satisfy its liability imposed by a domestic jurisdiction**
- ✓ **Paid by PTE ending after December 31, 2017 (TCJA)**

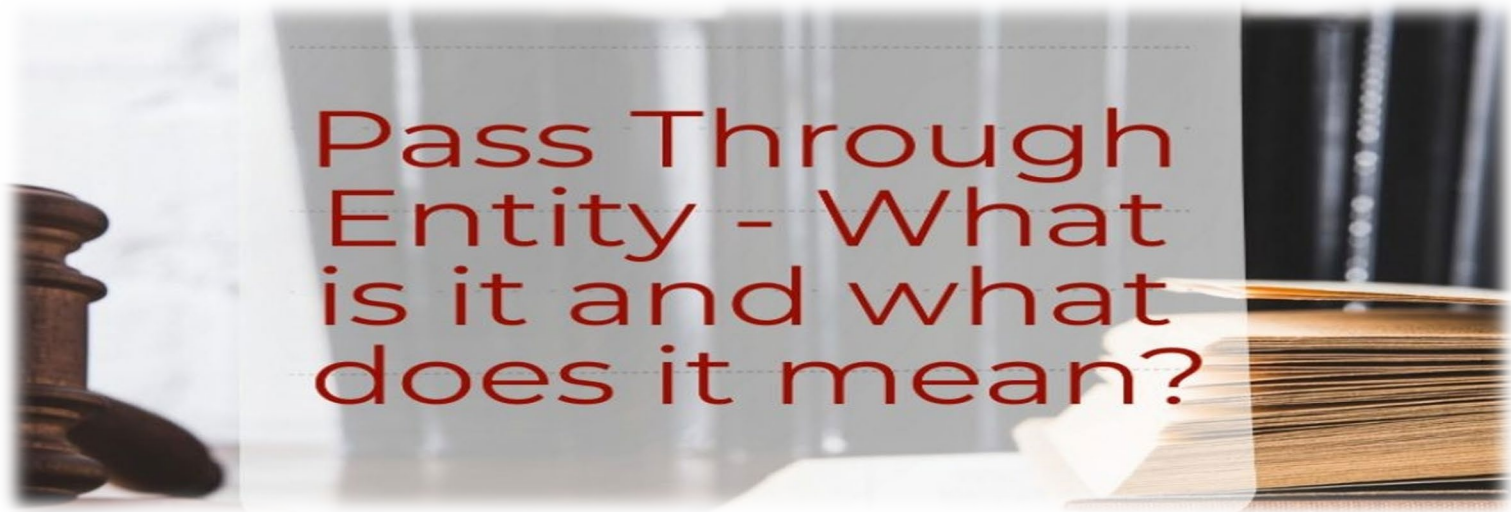
# February 2024 Solutions Room – PTET

## □ What are SITPs

- ✓ Deemed a § 164 deduction and not a § 212 expense
- ✓ Deemed to qualify as a § 164 deduction even when related to investment activities
- ✓ Language within 2020-75 suggests that the SITPs need not be related to a trade or business
- ❖ **Varies by States**

# February 2024 Solutions Room – PTET

- ❑ Due to TCJA \$10,000 SALT CAP, **states now offer PTET methods**



- ❑ **Tax imposed on entity itself vs. pass-through entity owners**

# February 2024 Solutions Room – PTET

## □ Fundamentals of PTET

- ✓ Entity pays state income tax on all income
- ✓ Elective or Mandatory
- ✓ Tax paid with return or by estimates
- ✓ PTET reduces ordinary income recorded in Box 1 of K-1
- ✓ PTET reduces taxpayer SE Tax on LLC/Partnership returns
- ✓ PTET reduces taxpayer AGI, assisting other tax provisions



# February 2024 Solutions Room – PTET

## □ Fundamentals of PTET

- ✓ Specified income tax payments (SITPs)
- ✓ Unlike the SALT limitation, PTET has no limit on the deduction



## Attendance Check #2

Please answer the poll in Zoom.  
If you are unable to enter your  
answer in the poll you can use  
the chat or Q&A box.



# February 2024 Solutions Room – PTET

- ❑ Advantages of PTET
  - ✓ Reduces pass-through income
  - ✓ Increase of other deductions
  - ✓ Increase of credits
  - ✓ Reduction of taxes





# February 2024 Solutions Room – PTET

## ❑ Not one size fits all

✓ Each state has different rules

✓ Less valuable at lower tax rates

✓ Residents vs nonresidents

✓ Refundable or Non-refundable credit



# February 2024 Solutions Room – PTET

## □ Example of PTET with Company ABC, LLC

- ✓ Company is a PTE
- ✓ Company has two members, both actively participate
- ✓ State PTET is elective annually
- ✓ State PTET is 6%

# February 2024 Solutions Room – PTET

## □ Example of PTET with Company ABC, LLC

- ✓ Company has net income before PTET of \$135,000
- ✓ PTET is  $\$135,000 \times 6\% = \$8,100$
- ✓ Ordinary Business Income will be \$126,900
  - $\$135,000 - \text{PTET } \$8,100 = \$126,900$

# February 2024 Solutions Room – PTET

## □ Example of PTET with Company ABC, LLC

- ✓ **Schedule K-1 (Form 1065) Box 1 for each member will be \$63,450.**
- ✓ **Schedule K-1 (Form 1065) Box 14a will be \$63,450**

# February 2024 Solutions Room – PTET

## □ Example of PTET with Company ABC, LLC

- ✓ Each member receives a state tax credit in the amount of 50% of the PTET
  - ❖ \$4,050 reported on members state Schedule K-1
  - ❖ Member reports this credit as a tax paid
    - i.e. estimated tax

# February 2024 Solutions Room – PTET

## □ Example of PTET with Company ABC, LLC

- ✓ Let's discuss advantages of paying the PTET



# February 2024 Solutions Room – PTET

## ❑ Deductible of SITP under IRS Notice 2020-75

✓ Is the deduction ‘above the line’

❖ Arriving at Adjusted Gross Income (AGI)

✓ Is the deduction ‘below the line’

❖ Itemized deduction

# February 2024 Solutions Room – PTET

## ❑ Deductible of SITP under IRS Notice 2020-75

- ✓ ‘above the line’
  - ❖ Directly connected to a trade or business
- ✓ Revenue Ruling 58-25
  - ❖ Tax imposed and paid by partnership on net profits of said PTE would be deductible in computing taxable income



# February 2024 Solutions Room – PTET

## ☐ State Income Tax refund and the Tax Benefit Rule

✓ IRC § 111



## Attendance Check #3

Please answer the poll in Zoom.  
If you are unable to enter your  
answer in the poll you can use  
the chat or Q&A box.



# February 2024 Solutions Room – PTET

## Who May Use

- ✓ Partnerships
- ✓ Multi-members LLCs
- ✓ S Corporations

# February 2024 Solutions Room – PTET

## ☐ Who May Not Use

### ✓ Sole proprietors

- Schedule C
- SMLLC

### ✓ Farmers

- Schedule F

# February 2024 Solutions Room – PTET

## ☐ Who May Not Use

### ✓ Farm Rentals

- Form 4835

### ✓ Landlords

- Schedule E

### ✓ C Corporations

- ✓ Form 1120

# February 2024 Solutions Room – PTET

**□ Business Entity Options that do not qualify for PTET**

**✓ What can be done?**

# February 2024 Solutions Room – PTET

- How Much is the PTET**
- What is a PTE Credit**
- Is the PTE Credit Refundable**
- What is a PTE Exclusion**
- How is Election made**
- What Forms need to be filed**

# February 2024 Solutions Room – PTET

## Estimated Payments

- ✓ Are they required by your state?
- ✓ When are they due?
- ✓ Will PTE be subject to estimated tax penalties?



## Attendance Check #4

Please answer the poll in Zoom.  
If you are unable to enter your  
answer in the poll you can use  
the chat or Q&A box.



# February 2024 Solutions Room – PTET

## □ PTET Example for DEF, LLC

- **Business income:** **\$78,000**
- **Net rental income:** **\$19,350**
- **Non qualified Dividend Income:** **\$ 6,050**

❖ **DEF, LLC has two members**

# February 2024 Solutions Room – PTET

## □ PTET Example for DEF, LLC

- **PTET @ 6% x (\$78,000 + \$19,550 + \$6,050)  
= \$6,216 tax**
- **Business Income of \$78,000 - \$6,216 =  
Ordinary business income of \$71,784**

# February 2024 Solutions Room – PTET

## Schedule K-1 (Form 1065)

Department of the Treasury  
Internal Revenue Service

# 2023

For calendar year 2023, or tax year

beginning  /  / 2023 ending  /  /

## Partner's Share of Income, Deductions, Credits, etc.

See separate instructions.

651123

OMB No. 1545-0123

Final K-1  Amended K-1

Part I Information About the Partnership	
A	Partnership's employer identification number
B	Partnership's name, address, city, state, and ZIP code DEF, LLC
C	IRS center where partnership filed return:
D	<input type="checkbox"/> Check if this is a publicly traded partnership (PTP)

Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items			
1	Ordinary business income (loss)	14	Self-employment earnings (loss)
	35,892		
2	Net rental real estate income (loss)		
	9,775		
3	Other net rental income (loss)	15	Credits
4a	Guaranteed payments for services		
4b	Guaranteed payments for capital	16	Schedule K-3 is attached if checked . . . . . <input type="checkbox"/>
4c	Total guaranteed payments	17	Alternative minimum tax (AMT) items
5	Interest income		
6	Ordinary dividends		
	3,025		

# February 2024 Solutions Room – PTET



# NAEA

› National Association  
of Enrolled Agents

## Office

*1730 Rhode Island Avenue, NW, Suite 400  
Washington, DC 20036, United States*

## Telephone

*(202) 822-6232*

## Email

*info@naea.org*

