

State Tax Observations

Massachusetts Enacts a Pass-Through Entity Tax

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Overriding Governor Charlie Baker's veto, the Massachusetts legislature recently enacted an elective pass-through entity tax (PTET). The legislation, originally passed in July, was vetoed by the governor in an effort to increase the refundable tax credit percentage. The Massachusetts PTET is a workaround intended to mitigate the \$10,000 federal limitation on the state and local tax (SALT) deduction imposed by the 2017 federal Tax Cuts and Jobs Act. The PTET is effective for years beginning on or after January 1, 2021.

Eligibility

A qualified pass-through entity (PTE) is eligible to make the election if:

- It is a partnership, an S-Corporation or limited liability company treated as an S-Corporation or partnership; and
- Its owners consist of (either resident or nonresident) individuals, fiduciaries, trusts or estates.

Annual Election

The election, which is irrevocable, is made with the timely filing of the original tax return, including extensions. An election made by the PTE is binding on all owners of the PTE, and individual owners cannot elect out of this tax.

Tax Rate

The PTET rate is a flat 5% which matches the Massachusetts individual income tax rate. The tax rate is applied to qualified income taxable in Massachusetts. Qualified income is the qualified member's aggregated taxable income included in such member's income.

Filing and Tax Due Date

The PTET for an electing PTE is due on the original, timely-filed tax return, which is due at the same time as the PTE's partnership information return or a corporate excise return.

Estimated Tax Payments

Additional guidance is needed for estimated tax payment requirements for tax years beginning January 1, 2021, the first year of the election. Many states have waived the requirement for estimated tax payments for the first year of the election. However, the total amount of the tax due must be paid by the filing deadline of the return, without regard to any extensions.

For tax years beginning on or after January 1, 2022, electing PTEs must make four equal installments due on April 15th, June 15th, September 15th and January 15th.

Refundable Tax Credit

A qualified PTE owner may claim a refundable credit for an amount equal to 90% of the tax paid on the owner's distributive share of the PTE's qualified net income.

Observations

The PTET is not applicable in a year where there is no federal limitation on that state and local tax deduction. Therefore, if the federal tax legislation changes with regard to SALT limitations or the SALT limitations expire, this PTET is no longer applicable.

Several unanswered questions remain regarding the Massachusetts PTET. For example, will the tax apply to tiered pass-through entities? Also, does the law provide for a tax credit for another state's PTET?

It is anticipated that the Massachusetts Department of Revenue (DOR) will issue regulations and guidance on the administration of the PTET in the coming weeks.

Contact Us

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