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Update on the new Oregon Pass-Through Entity – Elective Tax (PTE-E)

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In July 2021, Oregon established an elective Pass-Through Entity Tax (PTE-E), a business alternative income tax in response to the federal government's \$10,000 cap on the deduction of State and Local Taxes (SALT). The new tax, effective for tax years beginning on or after January 1, 2022, will allow for shareholders/partners to receive a deduction of state taxes.

The Oregon Department of Revenue has recently published guidance on implementation of this new favorable tax system. Please review the details of how it works and how it may benefit you this year.

Who does this apply to? A partnership, or S-corporation, or limited liability company electing to be treated as a partnership or S-corporation (and their shareholders/partners); it does not apply to Single Member LLCs or Sole Proprietorships.

What income is subject to tax by the eligible pass-through entity? The PTE will pay tax on the “distributive proceeds” of the entity. Distributive proceeds include net income, dividends, royalties, interest, rents, guaranteed payments, and gains of a PTE derived from or connected with sources within Oregon.

What are the tax rates?

- First \$250,000 of distributive proceeds – 9%
- Amount over \$250,000 of distributive proceeds – 9.9%

How does it save taxes? The entity will pay taxes to Oregon on the distributive proceeds that will later be passed through on Form K-1 to the shareholders/partners. By the entity paying the tax, it becomes a tax deduction and reduces the federal taxable income that flows through to the individual shareholder/partner's income tax return.

- For example, if an entity earned \$100,000 of distributive proceeds, this amount would have been reported on Form K-1 to the shareholders/partners in 2021.
- Under the new law, the entity can pay 9% of Oregon tax on the \$100,000, reducing the distributive proceeds to \$91,000.
- If the partner is in the 24% tax bracket, the savings would be \$2,160 on the federal individual income tax return, by having the entity pay the tax. (Please note this is a simplified example as it does not account for each individual taxpayer's specific variables.)
- On the individual Oregon tax return, Oregon will add back the \$9,000 paid to the state, putting the income back up to \$100,000. However, the \$9,000 tax payment made by the entity will be treated as a prepayment of tax on the Oregon individual tax return, therefore, giving full credit for the payment.
- This is a strategy to allow state taxes to be fully deductible whereas currently for most Oregon business owners, state and local taxes are not fully deductible due to the \$10,000 cap on tax deductions on Schedule A, Itemized Deductions.

Is the PTE-E mandatory? No, it is elective. The election must be made each year and is done by filing a timely PTE-E return, which for the 2022 calendar year would be due on April 15, 2023.

Is the election to pay the PTE-E tax revocable? Yes. The election can be revoked on or before the due date of the return, including extensions.

Are estimated tax payments required for the PTE-E tax? Yes. For 2022, the first estimate will be June 15th. Thereafter, payments are due September 15, 2022 and January 15, 2023. After that time, payments will be due April 15, June 15, September 15, and January 15, same as the individual estimated tax payment schedule.

How are estimated tax payments made for the PTE-E tax?

The entity will be required to register on Oregon's Revenue Online website before estimated tax payments can be made. Registration will open on June 6, 2022.

After registration, payment can be made using one of these options:

- Electronic payment using Revenue Online
- Mail a check and the OR-21-V voucher
- ACH Credit through Revenue Online

If an entity elects to pay the new PTE-E, can the owners still qualify for the reduced tax rate on Oregon qualified business income? Yes, this will not affect how the rules apply to the shareholder/partner.

How will this new entity tax interact with the Oregon individual estimated tax payments that have normally been paid?

- You will want to reduce the 2022 Oregon individual estimated tax payment requirement by the entity level tax payment.
- Since the first entity estimated tax payment is not available until June 15th, the entity may want to pay tax on earnings from January 1 – May 31 with the June payment.

What are the next steps?

- Determine if your entity, or the entity that you are a minority shareholder in, is going to use this new tax strategy.
- If you are a managing shareholder/partner, the first week of June, go to the *Resources* page of our website at <https://www.eblcpas.com/resources/> for the link of where to register your business. Between June 1st and June 15th, contact our firm and we will coordinate with you related to the amount of income and tax to be paid.
- If you are a minority shareholder/partner, prior to June 15th, find out from your entity how much tax has been paid on your behalf and then reduce your Oregon estimated tax payment by that amount.
- Our current plan is to advise individual taxpayers of the Oregon estimated tax payments that are needed for the year to be protected. Once entity level taxes have been paid, the Oregon individual income tax estimated payment amount should be reduced to reflect the entity level tax payments.
- **This is a fluid situation. More information will be provided as time goes by from the Oregon Department of Revenue as they implement this new program. The information provided above is based upon the information available at this time.**
- Please do not hesitate to contact us to review your specific situation.