

1 **INCOME TAX - PASS-THROUGH ENTITIES**

2 2012 GENERAL SESSION

3 STATE OF UTAH

4 **Chief Sponsor: Wayne L. Niederhauser**

5 House Sponsor: Patrick Painter

7 **LONG TITLE**

8 **General Description:**

9 This bill amends the Individual Income Tax Act to address provisions related to a
10 pass-through entity.

11 **Highlighted Provisions:**

12 This bill:

- 13 ▶ defines terms;
- 14 ▶ provides that a pass-through entity includes certain estates and trusts;
- 15 ▶ provides that a pass-through entity taxpayer includes certain beneficiaries of an
16 estate or trust;
- 17 ▶ addresses pass-through entity withholding exemptions;
- 18 ▶ provides that certain penalties and interest may not be imposed if a pass-through
19 entity that is a trust fails to pay or withhold an amount with respect to a dependent
20 beneficiary; ~~§~~ → [and]

20a ▶ establishes a rebuttable presumption for purposes of an audit; and ← ~~§~~

- 21 ▶ makes technical and conforming changes.

22 **Money Appropriated in this Bill:**

23 None

24 **Other Special Clauses:**

25 This bill takes effect for a taxable year beginning on or after January 1, 2013.

26 **Utah Code Sections Affected:**

27 AMENDS:



28 59-10-1402, as last amended by Laws of Utah 2009, Chapter 312

29 59-10-1403.2, as enacted by Laws of Utah 2009, Chapter 312



31 *Be it enacted by the Legislature of the state of Utah:*

32 Section 1. Section 59-10-1402 is amended to read:

33 **59-10-1402. Definitions.**

34 As used in this part:

35 (1) "Addition, subtraction, or adjustment" means:

36 (a) for a pass-through entity taxpayer that is classified as a C corporation for federal
37 income tax purposes, under Chapter 7, Corporate Franchise and Income Taxes:

38 (i) an addition to unadjusted income described in Section 59-7-105; or

39 (ii) a subtraction from unadjusted income described in Section 59-7-106;

40 (b) for a pass-through entity taxpayer that is classified as an individual, partnership, or
41 S corporation for federal income tax purposes:

42 (i) an addition to or subtraction from adjusted gross income described in Section
43 59-10-114; or

44 (ii) an adjustment to adjusted gross income described in Section 59-10-115; or

45 (c) for a pass-through entity taxpayer that is classified as an estate or a trust for federal
46 income tax purposes:

47 (i) an addition to or subtraction from unadjusted income described in Section
48 59-10-202; or

49 (ii) an adjustment to unadjusted income described in Section 59-10-209.1.

50 (2) "Business income" means income arising from transactions and activity in the
51 regular course of a pass-through entity's trade or business and includes income from tangible
52 and intangible property if the acquisition, management, and disposition of the property
53 constitutes integral parts of the pass-through entity's regular trade or business operations.

54 (3) "C corporation" is as defined in Section 1361, Internal Revenue Code.

55 (4) "Commercial domicile" means the principal place from which the trade or business
56 of a business entity is directed or managed.

57 (5) "Dependent beneficiary" means an individual who:

58 (a) is claimed as a dependent under Section 151, Internal Revenue Code, on another

59 person's federal income tax return; and

60 (b) is a beneficiary of a trust that is a pass-through entity.

61 [~~5~~] (6) "Derived from or connected with Utah sources" means:

62 (a) if a pass-through entity taxpayer is classified as a C corporation for federal income
63 tax purposes, derived from or connected with Utah sources in accordance with Chapter 7, Part
64 3, Allocation and Apportionment of Income - Utah UDITPA Provisions; or

65 (b) if a pass-through entity or pass-through entity taxpayer is classified as an estate,
66 individual, partnership, S corporation, or a trust for federal income tax purposes, derived from
67 or connected with Utah sources in accordance with Sections 59-10-117 and 59-10-118.

68 [~~6~~] (7) "Nonbusiness income" means all income of a pass-through entity other than
69 business income.

70 [~~7~~] (8) "Nonresident business entity" means a business entity that does not have its
71 commercial domicile in this state.

72 [~~8~~] (9) "Nonresident pass-through entity taxpayer" means a pass-through entity
73 taxpayer that is a:

74 (a) nonresident individual; or

75 (b) nonresident business entity.

76 [~~9~~-(a)] (10) "Pass-through entity" means a business entity that is:

77 [~~i~~] (a) the following if classified as a partnership for federal income tax purposes:

78 [~~A~~] (i) a general partnership;

79 [~~B~~] (ii) a limited liability company;

80 [~~C~~] (iii) a limited liability partnership; or

81 [~~D~~] (iv) a limited partnership;

82 [~~i~~] (b) an S corporation; [~~or~~]

83 (c) an estate or trust with respect to which the estate's or trust's income, gain, loss,
84 deduction, or credit is divided among and passed through to one or more pass-through entity
85 taxpayers; or

86 [~~iii~~] (d) a business entity similar to [~~Subsection (9)(a)(i) or (ii)] Subsections (10)(a)
87 through (c):~~

88 [~~A~~] (i) with respect to which the business entity's income, gain, loss, deduction, or
89 credit is divided among and passed through to one or more pass-through entity taxpayers; and

90 ~~[(B)]~~ (ii) as defined by the commission by rule made in accordance with Title 63G,
91 Chapter 3, Utah Administrative Rulemaking Act.

92 ~~[(b) "Pass-through entity" does not include an estate or trust that is classified as an~~
93 ~~estate or trust for federal income tax purposes.]~~

94 ~~[(10)]~~ (11) "Pass-through entity taxpayer" means a resident or nonresident individual, a
95 resident or nonresident business entity, or a resident or nonresident estate or trust:

96 (a) that is:

97 (i) for a general partnership, a partner;

98 (ii) for a limited liability company, a member;

99 (iii) for a limited liability partnership, a partner;

100 (iv) for a limited partnership, a partner;

101 (v) for an S corporation, a shareholder; ~~[or]~~

102 (vi) for an estate or trust described in Subsection (10)(c), a beneficiary; or

103 ~~[(vi)]~~ (vii) for a business entity described in Subsection ~~[(9)(a)(iii)]~~ (10)(d), a member,
104 partner, shareholder, or other title designated by the commission by rule made in accordance
105 with Title 63G, Chapter 3, Utah Administrative Rulemaking Act; and

106 (b) to which the income, gain, loss, deduction, or credit of a pass-through entity is
107 passed through.

108 ~~[(11)]~~ (12) "Resident business entity" means a business entity that is not a nonresident
109 business entity.

110 ~~[(12)]~~ (13) "Resident pass-through entity taxpayer" means a pass-through entity
111 taxpayer that is a:

112 (a) resident individual; or

113 (b) resident business entity.

114 ~~[(13)]~~ (14) "Return" means a return that a pass-through entity taxpayer files:

115 (a) for a pass-through entity taxpayer that is classified as a C corporation for federal
116 income tax purposes, under Chapter 7, Corporate Franchise and Income Taxes; or

117 (b) for a pass-through entity taxpayer that is classified as an estate, individual,
118 partnership, S corporation, or a trust for federal income tax purposes, under this chapter.

119 ~~[(14)]~~ (15) "S corporation" is as defined in Section 1361, Internal Revenue Code.

120 ~~[(15)]~~ (16) "Share of income, gain, loss, deduction, or credit of a pass-through entity"

121 means:

122 (a) for a pass-through entity except for a pass-through entity that is an S corporation:

123 (i) for a resident pass-through entity taxpayer, the resident pass-through entity

124 taxpayer's distributive share of income, gain, loss, deduction, or credit of the pass-through

125 entity as determined under Section 704 et seq., Internal Revenue Code; and

126 (ii) for a nonresident pass-through entity taxpayer, the nonresident pass-through entity

127 taxpayer's distributive share of income, gain, loss, deduction, or credit of the pass-through

128 entity:

129 (A) as determined under Section 704 et seq., Internal Revenue Code; and

130 (B) derived from or connected with Utah sources; or

131 (b) for an S corporation:

132 (i) for a resident pass-through entity taxpayer, the resident pass-through entity

133 taxpayer's pro rata share of income, gain, loss, deduction, or credit of the S corporation, as

134 determined under Sec. 1366 et seq., Internal Revenue Code; or

135 (ii) for a nonresident pass-through entity taxpayer, the nonresident pass-through entity

136 taxpayer's pro rata share of income, gain, loss, deduction, or credit of the S corporation:

137 (A) as determined under Section 1366 et seq., Internal Revenue Code; and

138 (B) derived from or connected with Utah sources.

139 (17) "Statement of dependent beneficiary income" means a statement:

140 (a) signed by the person who claims a dependent beneficiary as a dependent under

141 Section 151, Internal Revenue Code, on the person's federal income tax return for the taxable

142 year;

143 (b) attesting that the dependent is a dependent beneficiary; and

144 (c) indicating that the person expects that the dependent beneficiary's adjusted gross

145 income for the taxable year will not exceed the basic standard deduction for the dependent

146 beneficiary, as calculated under Section 63, Internal Revenue Code, for that taxable year.

147 Section 2. Section **59-10-1403.2** is amended to read:

148 **59-10-1403.2. Pass-through entity payment or withholding of tax on behalf of a**

149 **pass-through entity taxpayer -- Exceptions to payment or withholding requirement --**

150 **Procedures and requirements -- Failure to pay or withhold a tax on behalf of a**

151 **pass-through entity taxpayer.**

152 (1) (a) Except as provided in Subsection (1)(b), for a taxable year, a pass-through entity
153 shall pay or withhold a tax:

154 (i) on:

155 (A) the business income of the pass-through entity; and

156 (B) the nonbusiness income of the pass-through entity derived from or connected with
157 Utah sources; and

158 (ii) on behalf of a pass-through entity taxpayer.

159 (b) A pass-through entity is not required to pay or withhold a tax under Subsection

160 (1)(a):

161 (i) on behalf of a pass-through entity taxpayer who is a resident individual;

162 (ii) if the pass-through entity is an organization exempt from taxation under Subsection
163 59-7-102(1)(a); [~~or~~]

164 (iii) if the pass-through entity:

165 (A) is a plan under Section 401, 408, or 457, Internal Revenue Code; and

166 (B) is not required to file a return under Chapter 7, Corporate Franchise and Income
167 Taxes, or this chapter; or

168 [~~(iii)~~] (iv) if the pass-through entity is a publicly traded partnership:

169 (A) as defined in Section 7704(b), Internal Revenue Code;

170 (B) that is classified as a partnership for federal income tax purposes; and

171 (C) that files an annual information return reporting the following with respect to each

172 partner of the publicly traded partnership with income derived from or connected with Utah
173 sources that exceeds \$500 in a taxable year:

174 (I) the partner's name;

175 (II) the partner's address;

176 (III) the partner's taxpayer identification number; and

177 (IV) other information required by the commission.

178 (2) (a) Subject to Subsection (2)(b), the tax a pass-through entity shall pay or withhold
179 on behalf of a pass-through entity taxpayer for a taxable year is an amount:

180 (i) determined by the commission by rule made in accordance with Title 63G, Chapter
181 3, Utah Administrative Rulemaking Act; and

182 (ii) that the commission estimates will be sufficient to pay the tax liability of the

183 pass-through entity taxpayer under this chapter with respect to the income described in
184 Subsection (1)(a)(i) of that pass-through entity for the taxable year.

185 (b) The rules the commission makes in accordance with Subsection (2)(a):

186 (i) except as provided in Subsection (2)(c):

187 (A) shall:

188 (I) for a pass-through entity except for a pass-through entity that is an S corporation,
189 take into account items of income, gain, loss, deduction, and credit as analyzed on the schedule
190 for reporting partners' distributive share items as part of the federal income tax return for the
191 pass-through entity; or

192 (II) for a pass-through entity that is an S corporation, take into account items of
193 income, gain, loss, deduction, and credit as reconciled on the schedule for reporting
194 shareholders' pro rata share items as part of the federal income tax return for the pass-through
195 entity; and

196 (B) notwithstanding Subsection (2)(b)(ii)(D), take into account the refundable tax
197 credit provided in Section 59-6-102; and

198 (ii) may not take into account the following items if taking those items into account
199 does not result in an accurate estimate of a pass-through entity taxpayer's tax liability under this
200 chapter for the taxable year:

201 (A) a capital loss;

202 (B) a passive loss;

203 (C) another item of deduction or loss if that item of deduction or loss is generally
204 subject to significant reduction or limitation in calculating:

205 (I) for a pass-through entity taxpayer that is classified as a C corporation for federal
206 income tax purposes, unadjusted income as defined in Section 59-7-101;

207 (II) for a pass-through entity that is classified as an individual, partnership, or S
208 corporation for federal income tax purposes, adjusted gross income; or

209 (III) for a pass-through entity that is classified as an estate or a trust for federal income
210 tax purposes, unadjusted income as defined in Section 59-10-103; or

211 (D) a tax credit allowed against a tax imposed under:

212 (I) Chapter 7, Corporate Franchise and Income Taxes; or

213 (II) this chapter.

214 (c) The rules the commission makes in accordance with Subsection (2)(a) may
215 establish a method for taking into account items of income, gain, loss, deduction, or credit of a
216 pass-through entity if:

217 (i) for a pass-through entity except for a pass-through entity that is an S corporation,
218 the pass-through entity does not analyze the items of income, gain, loss, deduction, or credit on
219 the schedule for reporting partners' distributive share items as part of the federal income tax
220 return for the pass-through entity; or

221 (ii) for a pass-through entity that is an S corporation, the pass-through entity does not
222 reconcile the items of income, gain, loss, deduction, or credit on the schedule for reporting
223 shareholders' pro rata share items as part of the federal income tax return for the pass-through
224 entity.

225 (3) A pass-through entity shall remit to the commission the tax the pass-through entity
226 pays or withholds on behalf of a pass-through entity taxpayer under this section:

227 (a) on or before the due date of the pass-through entity's return, not including
228 extensions; and

229 (b) on a form provided by the commission.

230 (4) A pass-through entity shall provide a statement to a pass-through entity taxpayer on
231 behalf of whom the pass-through entity pays or withholds a tax under this section showing the
232 amount of tax the pass-through entity pays or withholds under this section for the taxable year
233 on behalf of the pass-through entity taxpayer.

234 (5) Notwithstanding Section 59-1-401 or 59-1-402, the commission may not collect an
235 amount under this section for a taxable year from a pass-through entity and shall waive [~~a~~] any
236 penalty [~~or~~] and interest on that amount if:

237 (a) the pass-through entity fails to pay or withhold the tax on the amount as required by
238 this section on behalf of the pass-through entity taxpayer;

239 (b) the pass-through entity taxpayer:

240 (i) files a return on or before the due date for filing the pass-through entity's return,
241 including extensions; and

242 (ii) on or before the due date including extensions described in Subsection (5)(b)(i),
243 pays the tax on the amount for the taxable year:

244 (A) if the pass-through entity taxpayer is classified as a C corporation for federal

245 income tax purposes, under Chapter 7, Corporate Franchise and Income Taxes; or

246 (B) if the pass-through entity taxpayer is classified as an estate, individual, partnership,
247 S corporation, or a trust for federal income tax purposes, under this chapter; and

248 (c) the pass-through entity applies to the commission.

249 (6) Notwithstanding Section 59-1-401 or 59-1-402, the commission may not collect an
250 amount under this section for a taxable year from a pass-through entity that is a trust and shall
251 waive any penalty and interest on that amount if:

252 (a) the pass-through entity fails to pay or withhold the tax on the amount as required by
253 this section on behalf of a dependent beneficiary;

254 (b) the pass-through entity applies to the commission; and

255 (c) (i) the dependent beneficiary complies with the requirements of Subsection (5)(b);

256 or

257 (ii) (A) the dependent beneficiary's adjusted gross income for the taxable year does not
258 exceed the basic standard deduction for the dependent beneficiary, as calculated under Section
259 63, Internal Revenue Code, for that taxable year; and

260 (B) the trustee of the trust retains a statement of dependent beneficiary income on
261 behalf of the dependent beneficiary.

261a **§→ (7) If a pass-through entity would have otherwise qualified for a waiver of a penalty and**
261b **interest under Subsection (6), except that the trustee of a trust has not applied to the**
261c **commission as required by Subsection (6)(b) or retained the statement of dependent**
261d **beneficiary income required by Subsection (6)(c)(ii)(B), it is a rebuttable presumption in an**
261e **audit that the pass-through entity would have otherwise qualified for the waiver of the penalty**
261f **and interest under Subsection (6). ←§**

262 Section 3. **Effective date.**

263 This bill takes effect for a taxable year beginning on or after January 1, 2013.

Legislative Review Note
as of 1-26-12 1:01 PM

Office of Legislative Research and General Counsel