



MULTISTATE INCOME/FRANCHISE TAX

Colorado enacts pass-through entity tax election Tax Alert

Overview

On June 23, 2021, Colorado Governor Jared Polis signed into law [House Bill 21-1327](#) (HB 1327), which is entitled the “SALT Parity Act” and provides for an election to impose income tax on S corporations and partnerships (pass-through entities or PTEs).

This Tax Alert summarizes some of the more significant provisions of HB 1327.

Summary of proposed pass-through entity tax election

- For tax years beginning on or after January 1, 2022, S corporations and partnerships, including limited liability corporations that are taxed as partnerships, may elect to be subject to Colorado income tax at the entity level for the tax year (PTE election). The PTE election is made annually and is binding on all electing pass-through entity owners. Electing pass-through entity owner means a shareholder of an S corporation or a partner in a partnership, except that a partner does not include a C corporation that is unitary with the partnership.
- The PTE election only applies to tax years beginning on or after January 1, 2022 in which there is a limitation on individual income tax deductions under Internal Revenue Code (IRC) section 164.
- The PTE tax rate is 4.55% which is the current income tax rate for C corporations and individuals. Additionally, electing PTE's are required to make estimated payments according to the corporate income tax estimated payment rules.
- For electing PTEs, the tax applies to each owner's pro rata or distributable share of income attributable to Colorado, plus Colorado resident owner's pro rata or distributable share of the PTE's income not attributable to Colorado.
- Any credits allowed under Colorado law that are attributable to the electing PTE should be claimed by the PTE and will not pass through to the owners. Any excess credits, net operating losses, or other tax

attributes of the PTE in an electing year will carry forward to subsequent years so long as the PTE makes the election in the subsequent year, subject to any other statutory limitations.

- The electing PTE owners should exclude any income from the electing PTE on their Colorado income tax return as they are not subject to tax on the portion of their income that was included in an electing PTE return. Furthermore, any individual owners are required to make an addition on their Colorado individual income tax return for any federal deductions allowed by IRC section 199A related to the electing PTE income.
- An electing PTE is entitled to a credit for taxes paid to other states whether the tax is paid by the PTE itself or the electing pass-through entity owners. The Colorado resident owners of an electing PTE are not entitled to take a credit for taxes paid to other states on the electing PTE's income.

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