



MULTISTATE INCOME/FRANCHISE TAX

North Carolina enacts changes to pass-through entity tax

Tax Alert

Overview

On April 3, 2023, North Carolina [Senate Bill 174](#) (S.B. 174) was enacted into law, which includes certain amendments to North Carolina's pass-through entity tax ("PTET").

This Tax Alert summarizes some of the provisions of S.B. 174.

North Carolina S.B. 174

Effective for tax years beginning on or after January 1, 2022:

- Allows a partnership with partners that are partnerships or S corporations to make the pass-through entity tax election. However, the distributive share of the electing partnership's income or loss allocated to partners that are partnership or S corporations is not included in the calculation of the PTET.
- Clarifies electing partnerships should continue to remit nonresident withholding on behalf of partners that are partnerships or S corporations.
- Allows a resident partner in a partnership that did not make the North Carolina PTET election to claim a credit equal to the amount of that partner's distributive share of entity-level income tax paid by the partnership to any other state or the District of Columbia. Under existing law, resident S corporation shareholders were already allowed to claim a credit for their share of entity-level income tax paid by the non-electing S corporation to any other state or the District of Columbia.
- For tax years beginning on or after January 1, 2022, but before January 1, 2023, resident partners or shareholders of a pass-through entity that made the North Carolina PTET election are not allowed to claim a credit for that partner's or shareholder's distributive share of entity-level income tax paid by the pass-through entity to any other state or the District of Columbia. Instead, the electing pass-through entity may

claim the credit against its PTET. The partners and shareholders may deduct their share of income or add their share of loss to the extent it was included in the electing pass-through entity's North Carolina taxable income.

Effective for tax years beginning on or after January 1, 2023:

- Modifies the calculation of the tax so that it is imposed on the sum of each partner's or shareholder's distributive share of income or loss attributable to North Carolina. The tax is no longer imposed on each resident partner's or shareholder's distributive share of the electing pass-through entity's income or loss both attributable and not attributable to North Carolina.
- Allows the following deductions for partners or shareholders of an electing pass-through entity:
 - A deduction is allowed for a partner's or shareholder's pro rata share of income attributable to North Carolina to the extent the income was included in the electing pass-through entity's North Carolina taxable income.
 - A deduction is allowed for a resident partner's or resident shareholder's pro rata share of income not attributable to North Carolina to the extent the income was included in the electing pass-through entity's taxable income in another state or the District of Columbia, which was subject to an entity-level tax.
- Resident partners or shareholders of an electing pass-through entity may not claim the credit for their distributive share of entity-level income tax paid by the pass-through entity to any other state or the District of Columbia as they are eligible for the deduction discussed above.
- Prohibits an electing entity from making the pass-through entity tax election or revoking the election after the return is filed.

Get in touch

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Have a question relating to this or any other pass-through entity tax regime? Reach out to one of our national multistate pass-through entity tax specialists.

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