



MULTISTATE INCOME/FRANCHISE TAX

## Recent guidance addressing New York's new pass- through entity tax Tax Alert

### Overview

On August 25, 2021, the New York State Department of Taxation and Finance ("Department") issued [TSB-M-21\(1\)C, \(1\)](#) ("TSB-M"), which provides guidance to taxpayers on the state's recently enacted elective pass-through entity tax ("PTET"). The TSB-M includes among other things, new details and instruction on New York's PTET election mechanics, tax computation, credit computation, estimated payments, and overpayments. This Tax Alert summarizes the recent guidance in the TSB-M.

Our prior Tax Alert providing a general overview of the New York PTET can be found [here](#).

### TSB-M guidance

New York's elective PTET is effective for tax years beginning on or after January 1, 2021, for partnerships and New York S corporations. Since the PTET's enactment in New York's 2021-2022 Budget Act on April 19, 2021, the TSB-M is the first guidance issued addressing specific aspects of the new regime. The TSB-M includes the highlights described below.

#### Election mechanics

For eligible entities with a calendar year, for 2021, the election must be made online by **October 15, 2021**. For calendar years after 2021, the annual election must be made by March 15 of the calendar year, at the same time that the first quarter estimated payment is due. An electing entity that is a fiscal-year taxpayer must elect, file, and pay PTET for the calendar year in which its fiscal year ends. The election, which is irrevocable for the tax year elected, must be made by an authorized person on behalf of the eligible entity through the entity's Online Business Services account. Entities which do not have an Online Business Services account will be required to make one at <https://www.tax.ny.gov/online/>. For tax year 2021, the website is open now through October 15, 2021; for tax year 2022, the online election may be made from January 1, 2022 through March 15, 2022.

## Return filing

The New York PTET return is due by March 15 after the close of the calendar year for all taxpayers. The PTET return for an electing entity with a fiscal year is due on or before March 15 following the close of the calendar year in which its fiscal year ends. The return is required to be filed online and can be extended six months. While the enabling statute permits amended returns with the consent/authorization of the commissioner, the TSB-M indicates no amendments are permitted for any reason.

## Pass-through entity taxable income

When elected, the New York PTET is imposed on income attributable to partners, members, or shareholders subject to tax under Article 22 (i.e., individuals, trusts and estates). Before computing its PTET taxable income, an electing partnership is required to classify all direct members or partners that are taxable under Article 22 as a resident or nonresident of New York.

- Members or partners may not be classified as part-year residents for PTET purposes. Instead, a member or partner will be treated as a New York resident if they were a resident of New York for at least half of the year in which the election applies.
- A trust's residency is classified by the residency of the trust and not the beneficiaries.

To compute its PTET taxable income, an electing partnership computes both a resident PTET taxable income pool and a nonresident PTET taxable income pool and adds these amounts together.

- If applicable, an electing partnership must take special allocations into account when computing each pool.
- The resident taxable income pool is computed by aggregating any amounts of income and gain that flow through to resident individual members or partners. For partnerships the resident pool is all income, but for S corporations the resident pool is only income sourced to New York.
- The TSB-M clarifies that this amount is offset by any losses or deductions that flow through to resident individual members or partners, without regard for any limitations that would be imposed on the member's or partner's federal and New York State personal income tax returns (e.g., passive activity loss or capital loss limitations). Including the losses reduces the tax base.
- Similarly, the nonresident taxable income pool is computed by aggregating any amounts of income and gain derived from or connected with New York sources that flow through to nonresident individual members or partners and offsetting that amount with New York source losses or deductions, without regard for any limitations.

## Claiming the PTET credit

- The TSB-M states that the credit is claimed by attaching Form IT-653, *Pass-Through Entity Tax Credit*, to the New York State personal income tax return.

- The credit cannot be claimed on composite returns -- Form IT-203-GR, *Group Return for Nonresident Partners*, or Form IT-203-S, *Group Return for Nonresident Shareholders of New York S Corporations*.
- An entity that files a PTET return should not also file a composite return as that may subject the partners, members, or shareholders to double taxation. As such, if an entity elects to file a PTET return, partners, members, and shareholders would not want to be included in a composite return for such entity.
- Trusts that are direct partners, members, or shareholders in an electing entity (other than a trust that is disregarded for tax purposes) are permitted to take a PTET credit on the trust's personal income tax return.
- The trust credit may not be distributed to the trust's beneficiaries.

### **Resident credit**

For tax years beginning on or after January 1, 2021, New York residents may also claim a credit for pass-through entity taxes paid to other states/localities/District of Columbia if they are "substantially similar" to the PTET. The Department indicates that it will provide a list of substantially similar taxes on its website.

### **Estimated payments**

Estimated tax payments may be made prior to December 31, 2021, using the Department's online estimated tax application which, per the TSB-M, will be made available by December 15, 2021. For the 2021 tax year, an electing entity is not required to make PTET estimated tax payments. However, the pass-through entity generally would need to pay its PTET liability (or be deemed to have paid under the so-called "recurring-item exception") during calendar year 2021 to qualify for the federal SALT tax workaround under Notice 2020-75 and to be deductible on the 2021 federal return of the pass-through entity. Regardless of whether an electing entity chooses to make optional estimated tax payments for tax year 2021, personal income tax estimated payments for 2021 required under Article 22 must be made by or on behalf of partners, members, or shareholders and calculated as if they were not entitled to the PTET credit.

For tax years beginning on or after January 1, 2022, an electing entity will be required to pay estimated tax using New York's online application. The required annual payment is equal to the lesser of 90% of the PTET required to be shown on the return of the electing entity for the taxable year, or 100% of the PTET shown on the return of the electing entity for the preceding PTET taxable year. If the PTET was not elected in the prior year, the required estimated payment is 90% of the PTET required to be shown on the return for the taxable year. PTET estimated payments may only be applied to the PTET (and not any other taxes) and payments may not be transferred between related entities or individuals.

### **Overpayments**

Overpayments reflected at the individual level are either refunded or credited forward on the individual partner's personal income tax return, without interest. If an electing entity's PTET taxable income is zero or less, the eligible taxpayers are not entitled to any PTET credits; rather, the electing entity may file an annual PTET return to request a refund of any PTET estimated tax payments it made.

## Considerations

With the tax year 2021 election deadline New York's PTET fast approaching on October 15, 2021, eligible entities should consider whether to elect into the new tax. For eligible entities with New York nonresident partners, members, or shareholders, it will be important to analyze the resident tax credit rules in those nonresident states to determine whether the election would result in a net benefit or detriment to the nonresidents. Given the irrevocability of the election for the tax year elected and the limitation on amending returns, electing entities may also wish to consider structuring alternatives to address the differing interests of the partners, members, or shareholders.

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