



SB 727– New Tax Treatment of PTE Income Distributed to Owners

Background

[Senate Bill 727 -2](#) is a methodology for addressing the limitation enacted in Section 164(b)(6) of the Internal Revenue Code on the deduction allowed for the deduction of state and local income taxes on personal income tax returns.

The bill, as amended, creates a new, elective entity level tax on an individual’s distributive share of income from a pass-through entity (PTE). The bill also creates a corresponding refundable credit that the individual will claim on their personal income tax return for the tax paid at the entity level.

This bill is similar to a law passed by the state of New Jersey for addressing the state and local tax limitation that has received approval from the IRS.

Implementation

Senate Bill 727 -2 applies to tax years beginning on or after January 1, 2022 and before January 1, 2024. Implementation of this new tax will include changes to the S Corporation and partnership programs as well as the individual income tax program. These changes have significant costs relating to implementation which include:

- Programming systems for a new tax program as well as updating current programs;
- Creating new and updating current tax forms, schedules, and instructions;
- Writing rules;
- Training staff and educating tax practitioners on the new program; and
- Working with software partners to update tax preparation programs.

In addition, this bill proposes complex coordination between the pass-through entity and the individual taxpayer owner regarding a refundable credit. This close coordination increases the administration costs for the department to track the payment of the tax to the credit claimed on the individual return. This additional tax program will also increase the burden on the entities to file additional forms and schedules as well as pay the additional tax.

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