



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2025 Biennium

Bill information:	
SB0554 - Provide optional pass-through entity tax with refundable credit (Hertz, Greg)	
Status:	As Introduced

- Significant Local Gov Impact
 Needs to be included in HB 2
 Technical Concerns
 Included in the Executive Budget
 Significant Long-Term Impacts
 Dedicated Revenue Form Attached

FISCAL SUMMARY

	<u>FY 2024</u> <u>Difference</u>	<u>FY 2025</u> <u>Difference</u>	<u>FY 2026</u> <u>Difference</u>	<u>FY 2027</u> <u>Difference</u>
Expenditures:				
General Fund	\$0	\$0	\$0	\$0
Revenue:				
General Fund	\$0	\$0	\$0	\$0
Net Impact-General Fund Balance:	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

Description of fiscal impact: SB 554 creates an optional pass-through entity tax that may be elected and paid by any pass-through entity filing a return in Montana. The pass-through entity tax would reduce some pass-through owners federal tax liability by allowing them to maximize their state and local tax deduction on their individual income tax returns but would have net zero fiscal impact on Montana tax liabilities, but could change the timing of receipts.

FISCAL ANALYSIS

Assumptions:

Department of Revenue

- SB 554 creates an optional pass-through entity tax (PTET) that may be elected and paid by any pass-through entity filing a return in Montana.
- Under current law, passthrough entities with non-resident owners are required to withhold tax or pay a composite tax (annually in March following the tax year) on behalf of the non-resident owners. The withholding tax can be claimed as a refundable credit on the owner's income tax return. The composite tax waives the nonresident owner filing requirement provided the nonresident owner does not have additional Montana source income.

3. Any pass-through entity may elect to pay this PTET on the distributive share of Montana source income allocated to residents and non-residents. For nonresident owners, the PTET overrides the current withholding system and composite tax requirements. The optional PTET incorporates characteristics of both the withholding tax and composite tax. It can be claimed as a refundable credit on the owner’s return or be in lieu of the nonresident owner’s return.
4. Paying the PTET at the entity level allows the owners to not have to pay at the individual level and therefore it does not count against the \$10,000 limitation on individual’s deduction of state and local taxes (SALT) at the federal level. This would result in a decrease in federal tax liability for many pass-through entity owners. This SALT deduction workaround has been implemented by many other states and has been allowed by the IRS through Notice 2020-75.
5. The PTET paid by these entities would then have to be added back into the federal taxable income on Montana individual income tax returns so Montana adjusted taxable income would not be impacted.
6. Electing pass-through entities would be required to make quarterly estimated payments for the PTET, and resident owners and any nonresident owners with other income in Montana would still be required to file an individual income tax return.
7. The owners of a pass-through paying the PTET may then claim a refundable credit on their individual income tax return for their share of the PTET paid and would still have to pay individual income tax on their pass-through income, so their total Montana tax liability would not change. This bill may cause some slight changes to the timing of payments related to pass-through income but is expected to have minimal fiscal impact to the state.
8. The Department of Revenue would have to make some changes to the pass-through tax form, pass-through payment voucher, and to the integrated revenue information system. It is expected that these changes can be made during normal maintenance. Additional workload and costs for the Department would be minimal.

Technical Notes:

Office of Budget and Program Planning

1. State revenue forecasters in states that have implemented SALT workarounds report difficulties separating SALT workaround and regular pass-through entity tax payments. Many of these SALT states report a very large increase in PTET inflows when SALT workarounds are implemented. These flows were difficult to reconcile with economic activity. This made revenue forecasting more challenging as the flows create the appearance of real increases in activity, but in time should have net zero effect. Like the changes from SB 399 (2021) this change will widen the confidence interval around the individual income tax forecast in the early years of PTET SALT workaround.

NO SPONSOR SIGNATURE

<i>Sponsor’s Initials</i>	<u>3/29/23</u> <i>Date</i>	 <i>Budget Director’s Initials</i>	<u>3-29-23</u> <i>Date</i>
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