

Understanding Iowa's New Pass Through Entity Tax (PTET)



What is the Pass Through Entity Tax (PTET)?

On May 11, 2023, Governor Reynolds signed [House File 352](#) which creates a voluntary election for a partnership or S corporation to be subject to Iowa income tax at the entity level. This is referred to as the Pass-Through Entity Tax (PTET). When the pass-through entity elects and pays the PTET, its owners receive a percentage of the PTET as a refundable tax credit on their personal income tax returns. The legislation applies retroactively to tax years beginning on or after January 1, 2022.

Which pass through entities are eligible to make a PTET election?

A business entity taxed as a partnership or S corporation for federal and Iowa income tax purposes and required to file a federal and Iowa partnership income tax return (Federal form 1065 and IA 1065) or federal and Iowa S corporation income tax returns (Federal form 1120-S and IA 1120S) may include an S corporation, general partnership, multi-member limited liability company (LLC), limited liability partnership (LLP), or limited partnership (LP).

A single-member LLC or other entity treated as a disregarded entity for federal and Iowa tax purposes is not eligible to make its own PTET election.

How does this Iowa tax change impact me?

The Issue: State taxes paid are practically non-deductible since the passing of the Tax Cuts & Jobs Act since most filers benefit from the standard deduction. Those who *do* itemize can only deduct up to \$10,000 for state and local taxes, including property taxes.

The Solution: Most states, now including Iowa, have created a way to deduct state income taxes paid without regard to the state and local tax (SALT) deduction limitation of \$10,000. Iowa pass through entities can make an annual election to pay their state income taxes at the entity level reducing taxable income that flows through to individuals.

If PTET is elected, the entity's new income tax is paid to the entity's Iowa tax account. Iowa refundable credits are then distributed back to the owners against their Iowa personal income tax in the same ratio as income is allocated to each owner. The PTET payment allows for an entity level deduction and reduces the income reported on the owners' K-1 in the tax year PTET is paid without regard to the SALT limitation.

The PTET cycle, when are the deadlines?

For tax year 2022, the PTET election and payment to the state of Iowa must be made **by April 30, 2024**.

For tax years 2023 and later, the PTET election and tax payment by the entity must be made by the due date for filing the pass-through entity's IA 1065 or IA 1120S income tax return.

- Pass-through entities will be allowed to make a PTET election for a tax year in one of two ways:
 - a. Make the election directly on the pass-through entity's IA 1065 partnership return or IA 1120S S corporation return.
 - b. Submit a PTET election form prior to filing the Iowa return by creating or logging into the pass-through entity's partnership or S corporation account on govconnect.iowa.gov

If 90% of PTET is paid by the original filing due date, an automatic six-month Iowa extension is granted. If an election is made via govconnect.iowa.gov, but 90% of PTET is not paid by the original due date, late file and late pay penalties will be assessed. If neither an election nor payment is made by the original due date, PTET is subject to rejection, and shareholder credits are subject to denial.

What's Next?

Basepoint Tax & Accounting stands ready to assist its clients with their analysis of their options under the PTET and complete all required elections before the deadlines based on the tax year they are required. Consult with your Basepoint Tax professional to understand more about this tax strategy and your scenario.

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