

# Electing Pass Through Entities

## **FAQ for Electing Pass-Through Entities – Updated June 30, 2022**

## **Updated Temporary Guidance for Electing Pass-Through Entities under Acts 2021-1 and 2021-423 (Updated June 14, 2021)**

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On Feb. 12, Governor Kay Ivey signed into law the Alabama Electing Pass-Through Entity Tax Act (Act 2021-1) which, beginning with the 2021 tax year, allows Alabama S-Corporations and Subchapter K entities (pass-through entities or PTEs) to elect to pay Alabama income tax at the entity level. Entities making this election (Electing PTEs) must notify ALDOR at any time during the tax year but no later than the 15th day of the third month following the close of that tax year for which the entity elects to be taxed as an Electing PTE. Entities making this election, including those that anticipate making this election for the 2021 tax year, may be required to begin making estimated payments on April 15, 2021.

### **General Guidance for Electing PTEs and Members**

1. If a pass-through entity elects to file and pay tax at the entity level, will it also be required to file a composite return and make composite payments for nonresident members/owners/partners?
  - ALDOR has the authority under Section 40-18-24.2(c)(3) to adopt rules to exempt an Electing PTE from the composite payment requirement for non-resident members. ALDOR plans to pursue adoption of a rule to this effect prior to the 2021 filing season.
2. Will nonresident members/owners/partners of an Electing PTE be required to file an Alabama nonresident individual tax return to report their distributive share of the income and the credit for the distributive share of taxes paid at the entity level?

– Act 2021-423 does not create a filing obligation for any member of an Electing PTE who would not otherwise have a filing obligation. Note, however, that a member seeking to claim the credit for taxes paid by the Electing PTE will have to file a return and report its distributive share of the income of the entity.

## **Estimated Payments for Electing PTEs**

The following temporary guidance is intended to help Electing PTEs determine whether, when, and how estimated payments should be made. Additional guidance regarding the election process, returns, and related matters will be issued prior to the 2021 filing season.

1. Under what circumstance will estimated payments be due for the 2021 tax year?

– If a PTE anticipates making the election for tax year 2021 and its estimated Alabama tax liability is expected to be \$500 or more, the PTE will be required to make estimated tax payments.

2. What are the due dates for estimated tax payments for the 2021 tax year?

### **Estimate tax due dates for calendar year filers:**

Payment 1 – April 15, 2021

Payment 2 – June 15, 2021

Payment 3 – September 15, 2021

Payment 4 – December 15, 2021

### **Estimate tax due dates for fiscal year filers:**

Will be due on the 15th day of the fourth, sixth, ninth, and 12th months of the fiscal year.

3. How do I calculate the amount of estimated quarterly tax payments due for the 2021 tax year?

– The required estimated quarterly payments will be 25% of the “required annual



payment.” The required annual payment generally means the lessor of 100% of the tax shown on the return for the taxable year or 100% of the tax shown on the return for the preceding tax year.

Except as noted below, this safe-harbor rule will apply to Electing PTEs making estimated payments for the 2021 tax year using the following calculations for the required annual payment:

**PTEs (other than S-Corporations):** Calculate the total of lines 1 through 17 in the Alabama column on Schedule K from the PTEs 2020 Form 65; then multiply this total by 5%.

**S-Corporations:** Calculate the total of lines 1 through 17 in the Alabama column on Schedule K from the S-Corporation’s 2020 Form 20S; then multiply this total by 5%.

**Please Note:** If an electing S-Corporation reported a loss on lines 1-17 in 2020, the safe-harbor rule will not apply.

#### 4. How can I pay the Electing PTE’s estimated tax installments?

– Estimated tax payments made by check should be submitted with the form [PTE-V](#) (</wp-content/uploads/2022/03/fptev.pdf>) and mailed to the address provided on this form.

Electronic payments can be made via ACH draft through [My Alabama Taxes](#) (<https://myalabamataxes.alabama.gov/>) and do not require the form PTE-V. Once logged into My Alabama Taxes, navigate to **Pass-Through Entity** under **Accounts** and click the **Make a Payment** link.

**Please Note:** Section 41-1-20, Code of Alabama 1975, requires all single tax pay of \$750 or more to be made electronically.

5. What if a PTE makes estimated payments and ultimately does not make the election to be an Electing PTE for this tax year?

– A refund may be requested by the entity. To request a refund, use the form [PTE-C \(/wp-content/uploads/2022/03/20fpfec.pdf\)](#) and list the amount of estimate payments made on line 5b.

## **Temporary Guidance for Waiver of Estimated Payment Penalties**

[Act 2021-423 \(https://arc-sos.state.al.us/ucp/LO621325.AI1.pdf\)](https://arc-sos.state.al.us/ucp/LO621325.AI1.pdf) was signed into law by Governor Ivey on May 14, 2021. The act provides that members of an Electing PTE are required to report their share of the income from the Electing PTE and in turn will be entitled to a refundable credit in an amount equal to their pro rata or distributive share of the Alabama income tax paid by the electing pass-through entity. To the extent that the retroactive effect of these provisions may have resulted in Electing PTEs and their members underpaying or failing to make the estimated tax payment due on April 15, 2021, the act authorizes ALDOR to waive any estimated tax penalties and interest associated with the underpayment.

The temporary guidance provided below is designed to address questions regarding the waiver of penalties authorized by Act 2021-423. ALDOR will issue more comprehensive guidance as needed on this subject ahead of the 2021 tax filing season, as well as guidance regarding the calculation of the credit for taxes paid by Electing PTEs, reporting of the credit by the entity and members, and related matters.

- 1. General Guidance for All Taxpayers** – If the underpayment is \$500 or less, no penalty will be incurred. If the underpayment is in excess of \$500, taxpayers may or may not be subject to a penalty. However, if the underpayment is due to the retroactive effect of the reporting provisions of Act 2021-423, taxpayers will be eligible for a waiver of any related penalty. More detailed information is provided below for specific taxpayers seeking a waiver of the penalty.

**Please Note:** The procedure for obtaining penalty relief may vary based on the organizational structure and filing status of the taxpayer seeking the relief. As a result, it is important to review the guidance below that corresponds to the status and organizational structure of the taxpayer seeking relief.

## FAQ

When should I request a waiver of penalties?

– Requests for waivers of penalties associated with estimated payments should be submitted at the time the taxpayer files their annual income tax or financial institution excise tax return using the penalty waiver request form (Form PWR) along with the estimated penalty forms identified below. The updated forms will be released in conjunction with the release of other forms for the 2021 filing season and will be available at [www.revenue.alabama.gov](https://www.revenue.alabama.gov) (<https://www.revenue.alabama.gov>).

What information should I include when submitting Form PWR?

– The following information should be included in the explanation section on the form:

- A reference to the provisions of Act 2021-423, along with the name and FEIN of the electing pass-through entity.
- The amount of estimated tax penalties as calculated by the taxpayer on Form 2210AL, 2220AL, or 2220E, as applicable.
- Any additional information relating to the taxpayer's circumstances, such as a change in the entity's decision regarding the pass-through entity election.

**2. Guidance for Individual Members/Owners/Partners** – If the first quarter estimate was not made or was underpaid, no penalty will be incurred if the

underpayment is made up by the due date of the second quarter estimate payment. If the underpayment is not made up by this time and the taxpayer is billed for a penalty, a waiver may be requested by submitting the 2021 Form PWR. Form PWR should be mailed separately from the return to the address on the form.

**Please Note:** The 2021 Form 2210AL should be used to calculate the penalty. The 2021 Form 2210AL should be submitted with the 2021 individual income tax return.

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If an individual has an underpayment attributable to the provisions of Act 2021-423 and other unrelated reasons, how should this be handled when computing the estimated tax penalty?

– The individual should complete Form 2210AL to calculate the penalty based on the entire underpayment. The penalty waiver only applies to the portion of the underpayment that is attributable to the provisions of Act 2021-423. In the explanation section of Form PWR, the individual should include the amount of underpayment and penalty attributable to the provisions of Act 2021-423.

If an individual made-up the first quarter underpayment by the second quarter due date, does the individual need to file Form 2210 AL and/or Form PWR?

– No.

**3. Guidance for Corporation Members/Owners/Partners** – If the underpayment is in excess of \$500, the corporation will need to file Form 2220 AL and submit it with the applicable corporate income tax return form. A penalty waiver may be requested by submitting 2021 Form PWR. Form PWR should be mailed separately from the return to the address on the form.

**Please Note:** The Form 2220AL contains a K1 exception checkbox that should be checked if the corporation's primary source of taxable income is from a K1. Corporations that meet the criteria for the K1 exception will not be required to compute a penalty, nor will they be billed a penalty.

4. **Guidance for Financial Institution Members/Owners/Partners** – If the underpayment is in excess of \$500, the financial institution will need to file the 2022 Form 2220E with the applicable financial institution excise tax form. A penalty waiver may be requested by submitting the 2022 Form PWR. Form PWR should be mailed separately from the return to the address on the form.
5. **Guidance for Electing Pass-Through Entities** – If the underpayment is in excess of \$500, the electing pass through entity will need to file the 2021 Form 2220AL and submit it with the electing pass through entity form. A penalty waiver may be requested by submitting the 2021 Form PWR. Form PWR should be mailed separately from the return to the address on the form.

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If an electing pass through entity did not make the first quarter estimate payment or has an underpayment that was made-up by the second quarter due date, does the electing pass through entity need to file Form 2220AL?

– Yes, Form 2220AL and the Form PWR should be filed.

## **Electing Pass-Through Entity FAQ (updated June 30, 2022)**

### **What entity types can elect to be treated as an Electing Pass-Through Entity?**

For tax years beginning on or after January 1, 2021, any Alabama S corporation, as is defined by Section 40-18-160, Code of Alabama 1975, and any Subchapter K Entity as is defined by Section 40-18-1, Code of Alabama 1975, may elect to be taxed as an Electing Pass-Through Entity.

### **How does the pass-through entity make an election to be treated as an Electing Pass-Through Entity?**

## Pass-Through Entity.

The pass-through entity **MUST** make the election to be treated as an Electing Pass-Through Entity by submitting the Pass-Through Entity Election, Form PTE-E, online via [My Alabama Taxes \(https://myalabamataxes.alabama.gov/\)](https://myalabamataxes.alabama.gov/).

Steps to Make Election:

- Log into My Alabama Taxes.
- Go to the Pass-Through Entity account.
- Click on the Update Election Status link.
- Follow the instructions to make the election.

The election is binding for that year and all subsequent tax years unless the entity properly elects to no longer be taxed as an Electing Pass-Through Entity. **Please note there is no paper equivalent of this online election.**

The election shall be accomplished by a vote by or written consent of the members of the governing body of the entity as well as a vote by or written consent of the owners/shareholders holding greater than 50 percent of the voting control of the entity, within the time prescribed above.

### **Can a Pass-Through Entity make an election to be treated as an Electing Pass-Through Entity simply by filing the tax return?**

No, the Electing Pass-Through Entity must submit Form PTE-E via [My Alabama Taxes \(https://myalabamataxes.alabama.gov/\)](https://myalabamataxes.alabama.gov/) at any time during the tax year or on or before the fifteenth day of the third month following the close of that tax year for which the entity elects to be taxed as an Electing Pass-Through Entity.

### **When is a Pass-Through Entity required to make the election for a tax year?**

Any time during the tax year or on or before the fifteenth day of the third month following the close of that tax year for which the entity elects to be taxed as an Electing Pass-Through

### **Is the date for making the election extended for the 2021 tax year?**



Yes, certain pass-through entities have until August 15, 2022, to submit Form PTE-E via [My Alabama Taxes \(https://myalabamataxes.alabama.gov/\)](https://myalabamataxes.alabama.gov/) to make a valid election for the 2021 tax year. ALDOR will recognize elections to be taxed at the entity level that are filed using My Alabama Taxes no later than August 15, 2022, as elections validly made by the due date for those pass-through entities who:

- Timely filed the required entity and member tax returns, as if the election had been properly made for the year;
- Timely made an Electing Pass-Through Entity extension payment; or
- Made an entity-level tax payment prior to the due date of the respective return.

### **Can a Pass-Through Entity revoke its election to be treated as an Electing Pass-Through Entity?**

The Electing Pass-Through Entity must submit Form PTE-E via [My Alabama Taxes \(https://myalabamataxes.alabama.gov/\)](https://myalabamataxes.alabama.gov/) at any time during a subsequent tax year or on or before the fifteenth day of the third month following the close of that tax year for which the entity elects to no longer be taxed as an Electing Pass-Through Entity. Once logged into My Alabama Taxes, the taxpayer will go to the Pass-Through Entity account and click on the Update Election Status link. The taxpayer will then follow the instructions to revoke the election.

### **What is the Electing Pass-Through Entity Tax return form and when is it due?**

Pass-through entities that file an election to be an Electing Pass-Through Entity must file Form EPT, in addition to Form 65 or 20S, and pay the tax due. The Pass-Through Entity's tax return is due on the 15th day of the third month after the close of the tax year (i.e. March 15 for calendar year filers).

### **Can a pass-through entity request an extension of time to file its tax return?**

If an extension has been granted for federal purposes, the extension is also granted for Alabama purposes; the Federal Form 7004 must be submitted with the Form 65/20S. The extension only applies to filing a return; no extensions are granted for payment of taxes due.

**NOTE:** This is an extension for filing purposes **ONLY**. The full amount of the tax liability is due by the **original** due date of the return. Payments should be submitted with Form PTE-V Pass Through Income Tax Voucher.

### **Are Pass-Through Entities that elect to pay the Electing Pass-Through Entity Tax required to make estimated tax payments?**

Yes, Electing Pass-Through Entities that have an Alabama income tax liability in excess of \$500 must pay estimated tax. An Electing Pass-Through Entity shall be subject to the provisions of Section 40-18-80.1, Code of Alabama 1975, (estimated tax for corporations). The required installments shall be 25 percent of the required annual payment. Required annual payment generally means the lesser of a) 100 percent of the tax shown on the return for the taxable year, or b) 100 percent of the tax shown on the return of the corporation for the preceding taxable year.

### **When are estimated tax payments due?**

#### **Estimate tax due dates for calendar year filers:**

Payment 1 – April 15

Payment 2 – June 15

Payment 3 – September 15

Payment 4 – December 15

#### **Estimate tax due dates for fiscal year filers:**

Will be due on the 15th day of the fourth, sixth, ninth, and 12th months of the fiscal year.

### **Will an entity be penalized if estimated tax payments are not made?**

Estimated tax payments not paid by each quarterly due date will be subject to interest on the underpayment – determined by applying the underpayment rate established by 26 U.S.C. §6621 (as provided by Alabama Code Section 40-18-80.1) to the underpayment for the period of underpayment. In addition, the 10% penalty provided for in Alabama Code Section 40-18-11 applies to estimated tax payments not paid by the quarterly due date.

#### **How do I make an estimate payment?**

## **How do I make an estimate payment?**

Estimated tax payments made by check should be submitted with the form [PTE-V](https://www.revenue.alabama.gov/wp-content/uploads/2020/12/fptev.pdf) (<https://www.revenue.alabama.gov/wp-content/uploads/2020/12/fptev.pdf>) and mailed to the address provided on this form. *Please Note: Section 41-1-20, Code of Alabama 1975 requires all single tax payments of \$750 or more to be made electronically.*

## **Electronic Payment Options Available:**

- **ACH Debit**– Taxpayers making e-payments via ACH Debit must have a Sign On ID and Access Code to login to [My Alabama Taxes](https://myalabamataxes.alabama.gov/) (<https://myalabamataxes.alabama.gov/>). Pre-registration is not necessary to make a payment on an invoice or assessment.
- **ACH Credit**– Taxpayers making e-payments via ACH Credit must be pre-approved by ALDOR. To register, complete and submit [Form EFT: EFT Authorization Agreement Form](https://revenue.alabama.gov/wp-content/uploads/2017/05/eft001.pdf) (<https://revenue.alabama.gov/wp-content/uploads/2017/05/eft001.pdf>).
- **Alabama Interactive**– ALDOR will accept e-payments for estimated payments through Alabama Interactive. Visit [Tax Estimation](http://www.alabamainteractive.org/taxestimation) (<http://www.alabamainteractive.org/taxestimation>).

## **What if a PTE makes estimated payments and does ultimately not make the election to be an Electing PTE for this tax year?**

A refund may be requested by the entity. To request a refund, use the form [PTE-C](https://revenue.alabama.gov/wp-content/uploads/2020/12/20fpotec.pdf) (<https://revenue.alabama.gov/wp-content/uploads/2020/12/20fpotec.pdf>) and list the amount of estimate payments made on line 5b.

## **How does the pass-through entity determine its tax liability? What is the entity-level tax rate?**

The Alabama taxable income of the Electing Pass-Through Entity will be calculated in accordance with Section 40-18-24 for Partnerships and Sections 40-18-161 and Section 40-18-162 for S Corporations. Taxable income shall be apportioned in accordance with the provisions of Chapter 27 of Title 40, Code of Alabama 1975. Use the total of total of lines 1 through

the Alabama column on Schedule K, Form 65, or Form 20S, to determine Alabama taxable income. Alabama tax paid under this provision shall not be deducted in calculating Alabama taxable income.

**The tax rate is 5%.**

**Are guaranteed payments included in the calculation of taxable income?**

Yes, taxable income includes guaranteed payments.

**Can an electing Pass-Through Entity claim a net operating loss?**

No, Pursuant to 40-18-24 and 40-18-161, NOLs are not considered in the calculation of net income.

**Can an owner, member, partner, or shareholder take a credit for taxes paid by the Electing Pass-Through Entity?**

The owner, member, partner, or shareholder of an electing pass-through entity shall be entitled to a refundable credit in an amount equal to its pro rata or distributive share of the Alabama income tax paid by the electing pass-through entity with respect to the corresponding tax year.

**Can an Electing Pass-Through Entity exclude income attributable to certain owners, i.e. tax-exempt owners, when calculating tax due?**

No, an Electing Pass-Through Entity's taxable income is calculated in accordance with the provisions 40-18-162, Code of Alabama 1975, as appropriate, and apportioned in accordance with the provisions of Section 40-18-27.

**Do owner's member, partner, or shareholders of an Electing Pass-Through Entity have a filing requirement?** Act 2021-423 does not create a filing obligation for any member of an Electing Pass-Through Entity who would not otherwise have a filing obligation. Note, however, that a member seeking to claim the credit for taxes paid by the Electing Pass-Through Entity will have to file a return and report its distributive share of the income of the entity.

**Can an Electing Pass-Through Entity claim Tax Incentive credits?**

The 2017 Alabama Historic Rehabilitation Tax Credit and the Railroad Modernization Act Credit must be claimed at the Electing Pass-Through Entity level and will not be passed through to the partners of the entity.

ALDOR requires the use of Schedule EPT-C, when claiming tax credits. The schedule allows the taxpayer to compute the total amount of tax credits allowable. The amounts entered on the Schedule EPT-C will carry over to the Form EPT, page 1. Many credits now must be claimed on the taxpayer's My Alabama Taxes account to receive the credit and the Schedule EPT-C attached to Form EPT. For more information on credits, please visit [ALDOR's Tax Incentives \(https://revenue.alabama.gov/tax-incentives/\)](https://revenue.alabama.gov/tax-incentives/) page and see instructions for Schedule EPT-C.

**Can an Electing Pass-Through Entity pass through Tax Incentive credits to its members?**

All credits except the 2017 Alabama Historic Rehabilitation Tax Credit and the Railroad Modernization Act Credit shall pass through to and may be claimed by an eligible taxpayer.

The Electing Pass-Through Entity would complete Schedule PC. The amounts entered on the Schedule PC will carry over to the Schedule K and K-1s. Many credits now must be claimed on the taxpayer's My Alabama Taxes account to receive the credit and the Schedule PC attached to Form 65 or 20S. For more information on credits, please visit [ALDOR's Tax Incentives \(https://revenue.alabama.gov/tax-incentives/\)](https://revenue.alabama.gov/tax-incentives/) page and see instructions for Schedule PC.

**Will an Electing Pass-Through Entity still be required to file a composite return, PTE-C, on behalf of nonresident members?** No, if an entity elects to be treated as an Electing Pass-Through Entity, the composite return is not required. If an election is not made, partnerships are required to make a composite payment in accordance with 40-18-24.2.

**Can a taxpayer transfer an overpayment from a composite return (Form PTE-C) to an Electing Pass-Through Entity's account?**

Yes, an overpayment from the prior year's composite return can be transferred to an Electing Pass-Through Entity's account.



**Can a Pass-Through Entity with all resident owners elect to be an Electing Pass-Through Entity?** Yes, any Alabama S corporation, as is defined by Section 40-18-160, Code of Alabama 1975, and any Subchapter K Entity as is defined by Section 40-18-1, Code of Alabama 1975, may elect to be taxed as an Electing Pass-Through Entity.

