

Stricken language would be deleted from and underlined language would be added to present law.

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# A Bill

HOUSE BILL 1209

By: Representatives Jett, *Lundstrum*

By: Senator J. Dismang

## For An Act To Be Entitled

AN ACT TO ALLOW ARKANSAS BUSINESSES TO REDUCE THEIR FEDERAL TAX BURDEN BY ELECTING ENTITY-LEVEL TAXATION; TO CREATE THE ELECTIVE PASS-THROUGH ENTITY TAX ACT; TO IMPOSE A TAX ON PASS-THROUGH ENTITIES; TO EXCLUDE CERTAIN INCOME FROM GROSS INCOME FOR PASS-THROUGH ENTITIES; AND FOR OTHER PURPOSES.

## Subtitle

TO CREATE THE ELECTIVE PASS-THROUGH ENTITY TAX ACT; TO IMPOSE A TAX ON PASS-THROUGH ENTITIES; AND TO EXCLUDE CERTAIN INCOME FROM GROSS INCOME FOR PASS-THROUGH ENTITIES.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF ARKANSAS:

SECTION 1. Arkansas Code § 26-51-404(b), concerning exemptions from gross income under the Income Tax Act of 1929, is amended to add an additional subdivision to read as follows:

(31)(A) For a person that is subject to the tax imposed under this chapter and that is a member of an affected business entity, an amount equal to the product of:

(i) The income subject to the tax paid under the Elective Pass-Through Entity Tax Act, § 26-65-101 et seq., by an affected business entity of which the person is a member; and

(ii) The person's pro rata interest, as reported to



the secretary under § 26-65-108, in the affected business entity of which the person is a member.

(B)(i)(a) A person that is subject to the tax imposed under this chapter as a resident or part-year resident and that is a member of an affected business entity may exclude from the taxable income subject to the tax imposed by this chapter the person's pro rata share of income subject to a tax paid to another state or the District of Columbia on income of any affected business entity of which the person is a member, if the taxes paid to the other state or the District of Columbia result from a tax that is substantially similar to the tax imposed under the Elective Pass-Through Entity Tax Act, § 26-65-101 et seq.

(b) A tax is substantially similar to the tax imposed under the Elective Pass-Through Entity Tax Act, § 26-65-101 et seq., if it is levied on the aggregate taxable income of each of the persons that have an ownership interest in an entity that is engaged in business for profit.

(ii) The amount excluded under this subdivision (b)(31) shall be calculated in a manner established by the secretary, which shall be consistent with § 26-51-504.

(C) With respect to a company that is a member of an affected business entity, the amount excluded under this subdivision (b)(31) is applied after all other applicable exclusions under this chapter and is not subject to any limits otherwise imposed by law.

(D) The exclusion under this subdivision (b)(31) does not apply to taxes imposed under the Arkansas Income Tax Withholding Act of 1965, § 26-51-901 et seq.

(E) As used in this subdivision (b)(31), "affected business entity" and "member" mean the same as defined in § 26-65-102.

SECTION 2. Arkansas Code Title 26 is amended to add an additional chapter to read as follows:

Chapter 65

Elective Pass-Through Entity Tax Act

26-65-101. Title.

This chapter shall be known and may be cited as the "Elective Pass-

Through Entity Tax Act".

26-65-102. Definitions.

As used in this chapter:

(1) "Affected business entity" means a business entity in which members that hold more than fifty percent (50%) of the voting rights in the business entity elect on an annual basis before the due date or extended due date of the business entity's income tax return to be taxed under this chapter;

(2) "Business entity" means an entity, including without limitation a general partnership, limited partnership, limited liability company, or for federal income tax purposes, a Subchapter S corporation, that:

(A) Is engaged in a business for profit; and

(B) Is required to file a return under this title;

(3) "Member" means a:

(A) Shareholder of a Subchapter S corporation;

(B) Partner in a general partnership, limited partnership, or limited liability partnership; and

(C) Member of a limited liability company;

(4) "Net operating loss" means the same as defined in § 26-51-427;

(5) "Pro rata interest" means a member's percentage of allocation of the profits of an affected business entity; and

(6) "Taxable year" means the same as defined in § 26-51-102.

26-65-103. Pass-through entity tax.

(a) Before the fifteenth day of the fourth month of the taxable year, an affected business entity shall pay to the Secretary of the Department of Finance and Administration the tax determined under this section.

(b)(1)(A) Except as provided in subdivision (b)(1)(B) of this section, a tax of five and nine-tenths percent (5.9%) is levied on the net taxable income of an affected business entity, as determined under Chapter 51 of this title, including any applicable basis adjustments, to the extent that the income is reported to the secretary as business income derived from the affected business entity.

(B) For an affected business entity that has a net capital gain, the rate of tax on the capital gain shall be fifty percent (50%) of the rate specified in subdivision (b)(1)(A) of this section.

(2) If the tax levied under subdivision (b)(1) of this section results in a net operating loss for an affected business entity, the affected business entity may carry forward the net operating loss in the same manner and for the same number of years as provided under § 26-51-427.

(3) An affected business entity that is a member of another affected business entity shall subtract its distributive share of the income or add its distributive share of the loss from the other affected business entity to the extent that the income or loss was derived from or connected with sources within this state.

(4) A nonresident individual who is a member of an affected business entity is not required to file an individual income tax return if, for the taxable year, the only source of income derived from or connected with sources within this state for the member or, if a joint income tax return is filed, the member and his or her spouse, is from one (1) or more affected business entities and each affected business entity files and pays the taxes due under this section.

(5) An affected business entity that files a return in Arkansas and has income from both within and without Arkansas shall apportion income to Arkansas under the Uniform Division of Income for Tax Purposes Act, § 26-51-701 et seq.

(6) An affected business entity that receives or earns a tax credit to be applied against the income tax imposed under Chapter 51 of this title may instead elect to apply the tax credit to reduce the tax imposed under this chapter, subject to any limitations applicable to the tax credit.

(c) An affected business entity shall report to the members of the affected business entity, for each taxable year, each member's respective pro rata share of the tax imposed under this section on the affected business entity based on the pro rata interest of each member as reported to the secretary under § 26-65-108.

26-65-104. Liability for tax.

(a) Except as otherwise provided in this section, an affected business entity is liable for the tax imposed under this chapter.

(b) If an affected business entity fails to pay the full amount of tax due under this chapter, the Secretary of the Department of Finance and Administration, in addition to assessing the affected business entity for the tax liability, may assess the individual members of the affected business entity based on the member's pro rata share of the income as determined by the member's pro rata interest.

26-65-105. Administration.

The Secretary of the Department of Finance and Administration shall administer and enforce this chapter in accordance with the Arkansas Tax Procedure Act, § 26-18-101 et seq.

26-65-106. Interest and penalty.

The interest and penalty provisions in the Arkansas Tax Procedure Act, § 26-18-101 et seq., apply to the tax imposed under this chapter.

26-65-107. Required annual payment.

(a) As used in this section, "required annual payment" means the lesser of:

(1) Ninety percent (90%) of the tax due under this chapter for the taxable year; or

(2) If the affected business entity filed a return for the preceding taxable year, one hundred percent (100%) of the tax due under this chapter as reported on that return.

(b)(1) An affected business entity that is required to pay tax under this chapter shall make a required annual payment each taxable year in four (4) estimated installments on the fifteenth day of the:

(A) Fourth month of the taxable year;

(B) Sixth month of the taxable year;

(C) Ninth month of the taxable year; and

(D) First month of the next succeeding taxable year.

(2) An affected business entity may elect to pay a required installment payment under this subsection before the date specified in subdivision (b)(1) of this section.

(3) Except as otherwise provided in this section, the amount of each installment payment required under this subsection shall be twenty-five

percent (25%) of the required annual payment.

(c)(1) If an affected business entity establishes that the affected business entity's annualized income installment calculated under subdivision (c)(3) of this section is less than the required annual payment, the required installment payment under this section is the annualized income installment.

(2) However, an affected business entity shall recapture a reduction in a required installment payment resulting under subdivision (c)(1) of this section by increasing:

(A) The amount of the next required installment payment by the amount of the reduction; and

(B) Subsequent required installment payments to the extent the reduction was not previously recaptured under this subsection.

(3) The annualized income installment under this section is the difference between:

(A) The product of:

(i) The tax imposed under this chapter for the taxable year that would be due if income subject to the tax imposed under this chapter for the months in the taxable year ending before the due date of the installment were annualized; and

(ii) The following percentage:

(a) For the first required installment payment, twenty-two and five-tenths percent (22.5%);

(b) For the second required installment payment, forty-five percent (45%);

(c) For the third required installment payment, sixty-seven and five-tenths percent (67.5%); and

(d) For the fourth required installment payment, ninety percent (90%); and

(B) The aggregate amount of any prior required installments for the taxable year.

(d)(1) Except as otherwise provided in this section, if an affected business entity makes an underpayment of estimated tax under this section, the penalties and interest provided for under § 26-18-208 shall be added to the tax imposed under this chapter.

(2) The amount of an underpayment under this subsection is the amount by which the required installment exceeds the amount, if any, of the

installment paid on or before the due date of the installment.

(3) A payment of estimated tax under this section shall be credited against unpaid or underpaid required installments in the order in which the installments are required to be paid.

(e) Payment of the estimated tax under this section or any required installment of estimated tax is a payment on account of the tax imposed under this chapter.

26-65-108. Report of pro rata interests.

(a) An affected business entity shall report on a form prescribed and furnished by the Secretary of the Department of Finance and Administration the pro rata interest of each member of the affected business entity.

(b) Unless a member of an affected business entity demonstrates the pro rata interests reported to the secretary to be fraudulent, the pro rata interests reported to the secretary are conclusive for purposes of computing a member's tax liability under this chapter and § 26-51-404(b)(31)(A).

SECTION 3. EFFECTIVE DATE. Sections 1 and 2 of this act are effective for tax years beginning on or after January 1, 2022.

*/s/Jett*