

## Important Notice Regarding North Carolina's Recently Enacted Pass-Through Entity Tax

On November 18, 2021, the North Carolina General Assembly enacted [Session Law 2021-180](#), the State's most recent budget bill. This new law contains a provision that allows certain pass-through entities ("PTEs") to elect to pay North Carolina income tax at the entity level (a "Taxed PTE").<sup>1</sup> North Carolina now joins several other states that have enacted legislation meant to reduce the impact of the federal state and local tax ("SALT") deduction cap on an individual's federal income tax return.<sup>2</sup>

The purpose of this notice is to provide answers to frequently asked questions ("FAQs") related to North Carolina's new law. These FAQs are intended to provide general information to taxpayers and tax professionals. Accordingly, these FAQs may be updated or modified.

The following topics are addressed in this notice:

### Topic A: General Information

- A1. Can you summarize North Carolina's new Taxed Pass-Through Entity law?
- A2. When is North Carolina's Taxed PTE law effective?
- A3. What type of entity is eligible to make the Taxed PTE Election?
- A4. How can an eligible PTE make the Taxed PTE Election?
- A5. Can a Taxed PTE revoke the Taxed PTE Election? If so, how?
- A6. How does a Taxed PTE calculate its North Carolina taxable income?
- A7. How does a Taxed PTE calculate its North Carolina income tax?
- A8. When is the filing deadline for a Taxed PTE to file its NC Tax Return?
- A9. Is a Taxed PTE required to pay estimated income tax payments?
- A10. When does a Taxed PTE have to pay estimated income tax?
- A11. For tax year 2022, the first year a PTE can make the Taxed PTE Election, will a PTE that makes the Taxed PTE Election be subject to interest for underpayment of estimated income tax?
- A12. Can a Taxed PTE file an NC Tax Return and remit North Carolina tax payments electronically?
- A13. Can a Taxed PTE request a refund of an overpayment of the PTE Tax?
- A14. What are the relevant reporting requirements for a Taxed PTE to its Owners?

### Topic B: Owner of Taxed PTE and the NC Tax Return

- B1. How does an Owner of a Taxed PTE account for the income of the PTE on their individual NC Tax Return?

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<sup>1</sup> See SB 105, s. 42.5.(a-n); [S.L. 2021-180](#).

<sup>2</sup> The "SALT cap" was added to federal law in 2017 as part of [Tax Cuts and Jobs Act](#).

- B2. I am an Owner of a PTE. The PTE plans to make the Taxed PTE Election. The PTE voluntarily pays North Carolina income tax based on the estimated net income of the PTE. How does that impact me as the Owner of the PTE?
- B3. I am an Owner of a Taxed PTE. When calculating the North Carolina taxable income of the Taxed PTE, the Taxed PTE included a North Carolina decoupling adjustment to federal gross income. When I calculate my North Carolina taxable income, am I required to include the same North Carolina decoupling adjustment?
- B4. I am an Owner of a Taxed PTE. I have become aware that the Taxed PTE did not pay the full amount of tax shown due on the Taxed PTE’s NC Tax Return. How does that impact me as an Owner of the Taxed PTE?
- B5. I am an Owner of a Taxed PTE. I was allocated a net loss from the Taxed PTE for the tax year. How do I account for this loss on my NC Tax Return?
- B6. Is a nonresident Owner of a Taxed PTE required to file an NC Tax Return?

**Topic C: Owner of a Taxed PTE and North Carolina Income Tax Credits**

- C1. I am a North Carolina resident Owner of a Taxed PTE. Can I claim a tax credit for income taxes paid to another state by the Taxed PTE on my NC Tax Return?
- C2. I am a North Carolina resident Owner of a Taxed PTE. The Taxed PTE does business in North Carolina and State XYZ. State XYZ does not allow the PTE to pay income tax at the entity level. As an Owner, I filed an income tax return in State XYZ and paid income tax to that state. Can I claim the tax credit for income taxes paid to State XYZ on my NC Tax Return?
- C3. I am a North Carolina resident Owner of a PTE. The PTE did not make the Taxed PTE election. The PTE does business in North Carolina and State XYZ. The PTE filed an income tax return and paid income tax in State XYZ. Can I claim the tax credit for income taxes paid to another state by the PTE on my NC Tax Return?
- C4. I am an Owner of a Taxed PTE. Are there any special rules on who can claim a North Carolina income tax credit?

**Topic A. General Information**

**A1. Can you summarize North Carolina’s new Taxed Pass-Through Entity law?**

The 2021 General Assembly added or revised several statutes within [Article 4 of Chapter 105](#) to allow an eligible S Corporation and an eligible partnership to elect to be taxed for North Carolina income tax purposes at the entity level (a “Taxed S Corporation,” a “Taxed Partnership,” and collectively a “Taxed PTE”).<sup>3</sup> If a PTE makes a timely election to pay North Carolina income tax as a Taxed PTE (“the Taxed PTE Election”), the Taxed PTE pays income tax on the share of income for all of its shareholders or partners (collectively, “Owners”).

The tax on the Taxed PTE is imposed at the individual income tax rate for the applicable taxable year.<sup>4</sup> Each Owner of the Taxed PTE is allowed to deduct the Owner’s share of the Taxed PTE’s income on the Owner’s North Carolina income tax return (“NC Tax Return”).

<sup>3</sup> See SB 105, s. 42.5.(f); [S.L. 2021-180](#).

<sup>4</sup> See [N.C. Gen. Stat. § 105-153.7\(a\)](#).

North Carolina law expressly provides that when a PTE elects to be a Taxed PTE, the State's income tax is imposed on the taxable income of the PTE itself (and not the taxable income of the individual Owner).<sup>5</sup> Under current federal law, a PTE that elects to pay state income tax at the entity level (as opposed to the Owner level) may generally deduct the full amount of its state income tax as a business expense on the PTE's federal income tax return.

## **A2. When is North Carolina's taxed PTE law effective?**

An eligible PTE can make the Taxed PTE Election by timely filing an NC Tax Return for a tax year that begins on or after January 1, 2022.<sup>6</sup>

## **A3. What type of entity is eligible to make the Taxed PTE Election?**

An eligible S Corporation required to file an NC Tax Return under [N.C. Gen. Stat. § 105-131.7](#) and an eligible partnership required to file an NC Tax Return under [N.C. Gen. Stat. § 105-154\(c\)](#) can make the Taxed PTE Election. An entity that is not a PTE is not eligible to make the Taxed PTE Election.

In North Carolina, an eligible S Corporation is an S Corporation as defined under North Carolina law.<sup>7</sup> An eligible partnership is defined as a domestic partnership, a foreign partnership, or a limited liability company ("LLC") that is classified for federal income tax purposes as a partnership.<sup>8</sup> The following partnerships are not eligible to make an election to be a Taxed Partnership:<sup>9</sup>

- A publicly traded partnership that is described in section 7704(c) of the Code.
- A partnership that has at any time during the taxable year a partner who is not one of the following:
  - (1) An individual.
  - (2) An estate.
  - (3) A trust described in section 1361(c)(2) of the Code.
  - (4) An organization described in section 1361(c)(6) of the Code.

## **A4. How can an eligible PTE make the Taxed PTE Election?**

Beginning with tax year 2022, an eligible PTE has the option to make the Taxed PTE Election [on its timely filed annual NC Tax Return](#). The Taxed PTE Election is for the tax year covered by the return. Importantly, the Taxed PTE Election must be made by the due date of the PTE's annual return, including extensions. A Taxed PTE Election on a late-filed NC Tax Return is not valid. The Department will provide guidance on how to make the Taxed PTE Election when the Department publishes the instructions for the applicable 2022 NC Tax Return.

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<sup>5</sup> See SB 105, s. 42.5.(c,h); [S.L. 2021-180](#).

<sup>6</sup> See SB 105, s. 42.5.(n); [S.L. 2021-180](#).

<sup>7</sup> See SB 105, s. 42.5.(a,c); [S.L. 2021-180](#). See also [N.C. Gen. Stat. § 105-131\(b\)\(8\)](#).

<sup>8</sup> See SB 105, s. 42.5.(f); [S.L. 2021-180](#). See also [N.C. Gen. Stat. § 105-153.3\(b\)\(13\)](#).

<sup>9</sup> See SB 105, s. 42.5 (h); [S.L. 2021-180](#).

For example:

- An eligible S Corporation filing a calendar year NC Tax Return intends to make the Taxed PTE Election for tax year 2022. The S Corporation is granted an extension to file its NC Tax Return. The S Corporation files the NC Tax Return on or before October 15, 2023, and marks the Taxed PTE Election box on the front page of the return. The Taxed PTE Election is valid.
- An eligible partnership filing a calendar year NC Tax Return intends to make the Taxed PTE Election for tax year 2022. The partnership was not granted a federal or North Carolina extension. The partnership files the NC Tax Return on October 15, 2023, and marks the Taxed PTE Election box on the front page of the return. The Taxed PTE Election is not valid.

**A5. Can a Taxed PTE revoke the Taxed PTE Election? If so, how?**

Yes. A Taxed PTE can revoke the Taxed PTE Election if an authorized person requests the revocation prior to the due date of the NC Tax Return, including any extensions. The Taxed PTE Election cannot be revoked after the due date of the NC Tax Return for the PTE. The Department will provide guidance on how to revoke the Taxed PTE Election when the Department publishes the instructions for the applicable 2022 NC Tax Return.

For example:

- An eligible partnership files a calendar year NC Tax Return for tax year 2022 on March 15, 2023, and makes the Taxed PTE Election. The partnership was not granted a federal or North Carolina extension. The partnership files an amended NC Tax Return on April 15, 2023, and revokes the Taxed PTE Election. The revocation of the Taxed PTE Election is valid. The revocation cannot be further changed since the partnership filed an amended NC Tax Return revoking the Taxed PTE Election on the original due date of the NC Tax Return and the partnership was not granted an extension to file the NC Tax Return.
- An eligible S Corporation is granted an extension of time to file its NC Tax Return for tax year 2022. On September 15, 2023, the S Corporation files a calendar year NC Tax Return for tax year 2022 and makes the Taxed PTE Election. The S Corporation files an amended NC Tax Return on October 15, 2023, and revokes the Taxed PTE Election. The revocation of the Taxed PTE Election is valid. The revocation cannot be further changed since the S Corporation filed an amended NC Tax Return revoking the Taxed PTE Election on the extended due date of the NC Tax Return.

**A6. How does a Taxed PTE calculate its North Carolina taxable income?**

The North Carolina taxable income of a Taxed PTE is determined by adding the following:

1. Each Owner's share of the Taxed PTE's income or loss, subject to the adjustments provided in [N.C. Gen. Stat. §§ 105-153.5](#) and [105-153.6](#), attributable to North Carolina, and
2. Each resident Owner's share of the Taxed PTE's income or loss, subject to the adjustments provided in [N.C. Gen. Stat. §§ 105-153.5](#) and [105-153.6](#), not attributable to North Carolina.

Importantly, separately stated items of deduction are not included when calculating each Owner's share of the Taxed PTE's taxable income. In addition, the adjustments required by [N.C. Gen.](#)

[Stat. § 105-153.5\(c3\)](#) (for Owners of Taxed PTEs) are not included in the calculation of the Taxed PTE's taxable income.<sup>10</sup>

**A7. How does a Taxed PTE calculate its North Carolina income tax?**

A Taxed PTE calculates its North Carolina income tax by multiplying its North Carolina taxable income by the tax rate imposed on individuals who are required to file an NC Tax Return.<sup>11</sup>

**A8. When is the filing deadline for a Taxed PTE to file its NC Tax Return?**

A Taxed PTE must file its NC Tax Return by the due date of the applicable NC Tax Return for the PTE. Without a valid extension, the due date of the NC Tax Return for an S Corporation and for a partnership is the 15th day of the 4th month following the PTE's year end. For example, for a calendar year Taxed Partnership, Form D-403 must be filed by April 15th.

A PTE that is granted an automatic extension to file a federal income tax return will be granted an automatic extension to file its corresponding NC Tax Return if the PTE certifies on its NC Tax Return that the PTE received an automatic federal extension.

If a PTE is not granted an automatic federal extension to file a federal income tax return, the PTE may still request an extension of time to file its NC Tax Return by filing the applicable North Carolina extension form by the original due date of the PTE's NC Tax Return.

**A9. Is a Taxed PTE required to pay estimated income tax payments?**

Yes. A Taxed PTE that can reasonably expect to have a North Carolina income tax liability of at least five hundred dollars (\$500) is required to pay estimated tax payments in the same manner as a C corporation.<sup>12</sup> The Department will post a new form on its website soon.

**Note:** A PTE that plans to make the Taxed PTE Election in tax year 2022 may voluntarily pay North Carolina income tax based on the estimated net income of the PTE. The PTE will use the same form that a Taxed PTE uses to make estimated tax payments.

**A10. When does a Taxed PTE have to pay estimated income tax?**

A Taxed PTE required to pay estimated income tax generally must make estimated tax payments in four equal installments. The installments are generally due on or before the 15th day of the fourth, sixth, ninth and twelfth months of the taxable year (for calendar year filers, April 15, June 15, September 15, and December 15). If the due date of the payment falls on a weekend, national or State holiday, a payment postmarked by the day following that holiday or weekend is considered timely.<sup>13</sup>

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<sup>10</sup> See SB 105, s. 42.5.(c,h), [S.L. 2021-180](#).

<sup>11</sup> See SB 105, s. 42.5.(c,h), [S.L. 2021-180](#).

<sup>12</sup> See SB 105, s. 42.5.(m); [S.L. 2021-180](#).

<sup>13</sup> See [Directive TA-18-1](#).

**A11. For tax year 2022, the first year a PTE can make the Taxed PTE Election, will a PTE that makes the Taxed PTE Election be subject to interest for underpayment of estimated income tax?**

No. The Taxed PTE will not be subject to interest for underpayment of estimated income tax for tax year 2022.

**A12. Can a Taxed PTE file an NC Tax Return and remit North Carolina tax payments electronically?**

It depends. The Department provides [eFile software providers](#) with the specifications needed to produce NC Tax Returns electronically. To the extent an approved eFile software provider produces 2022 NC Tax Returns for applicable PTEs, a Taxed PTE may file its NC Tax Return (and remit tax payments) electronically. The Department encourages taxpayers to take advantage of electronic filing options, when available, to ensure the efficient and accurate processing of returns and payments.

**A13. Can a Taxed PTE request a refund of an overpayment of the PTE Tax?**

Yes. When a Taxed PTE files an NC Tax Return reflecting an overpayment due the Taxed PTE, the Department must refund the overpayment within the provisions of [N.C. Gen. Stat. § 105-241.7](#).

**Important:** Only the Taxed PTE, not its Owners, are entitled to request a refund of an overpayment.<sup>14</sup>

**A14. What are the relevant reporting requirements for a Taxed PTE to its Owners?**

In addition to the applicable federal and State reporting requirements for partnerships and S Corporations (e.g., each Owner's share of the PTE's income, adjustments, tax credits, etc.), a Taxed PTE must also report to its Owners:

1. That it made the election to be a Taxed PTE; and
2. The amount of the Owner's share of income or loss from the Taxed PTE to the extent it was included in the Taxed PTE's North Carolina taxable income; and
3. The amount of tax paid by the Taxed PTE on the Owner's share of the Taxed PTE's North Carolina taxable income.

**Note:** The Department will provide additional guidance and instructions on the various reporting requirements for Taxed PTEs when the Department publishes the instructions for the applicable 2022 NC Tax Return.

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<sup>14</sup> See SB 105, s. 42.5.(c,h), [S.L. 2021-180](#).



## **Topic B: Owner of Taxed PTE and the NC Tax Return**

### **B1. How does an Owner of a Taxed PTE account for the income of the PTE on their individual NC Tax Return?**

A taxpayer that is an Owner of a Taxed PTE may deduct the amount of the taxpayer's share of income from the Taxed PTE to the extent it was included in the Taxed PTE's North Carolina taxable income and the taxpayer's adjusted gross income.<sup>15</sup>

**Note:** The Department will provide additional guidance and instructions (including which line the Owner must use to report the deduction) in the instructions for the applicable 2022 NC Tax Return.

### **B2. I am an Owner of a PTE. The PTE plans to make the Taxed PTE Election in tax year 2022. The PTE voluntarily pays North Carolina income tax based on the estimated net income of the PTE. How does that impact me as the Owner of the PTE?**

It depends. If an Owner of a PTE fails to include the Owner's share of income from the PTE in the Owner's calculation of North Carolina estimated tax for tax year 2022, the Owner will not owe estimated tax interest on the Owner's share of the PTE's income so long as the PTE does the following:

1. Meets the statutory requirements to be a Taxed PTE in North Carolina for tax year 2022, and
2. Makes the Taxed PTE Election on its NC Tax Return for tax year 2022.

If the PTE is not a Taxed PTE for tax year 2022, the Owner of the PTE must include their share of the PTE's income for tax year 2022 in their determination of whether the Owner was required to pay North Carolina estimated tax. The Owner may be subject to interest on any underpayment of estimated tax.<sup>16</sup>

If, during tax year 2022, the PTE decides it will not make the Taxed PTE Election, the Owner of the PTE may be eligible to use the annualized installment method for calculating estimated tax installments authorized in [N.C. Gen. Stat. § 105-163.15\(e\)](#).

### **B3. I am an Owner of a Taxed PTE. When calculating the North Carolina taxable income of the Taxed PTE, the Taxed PTE included a North Carolina decoupling adjustment to federal gross income. When I calculate my North Carolina taxable income, am I required to include the same North Carolina decoupling adjustment?**

Except as specifically excluded by statute, the adjustments provided in [N.C. Gen. Stat. §§ 105-153.5](#) and [105-153.6](#) are included in the calculation of the tax imposed on Taxed PTEs.<sup>17</sup>

The required North Carolina adjustments, even when included in the amount of tax calculated for the Taxed PTE, must also be passed-through and reported on the Owners' NC Tax returns.

<sup>15</sup> See SB 105, s. 42.5.(i), [S.L. 2021-180](#).

<sup>16</sup> See [N.C. Gen. Stat. § 105-163.15\(a\)](#).

<sup>17</sup> See SB 105, s. 42.5.(c,h), [S.L. 2021-180](#). See also [Question A6](#).

For example:

Partner A is a partner in Partnership XYZ. Partner A’s distributive share of North Carolina income from Partnership XYZ is \$1,000, which includes \$800 of business income and a North Carolina addition of \$200 to account for bonus depreciation deducted on the federal return. Partnership XYZ is a Taxed Partnership. Taxed Partnership XYZ calculates and pays North Carolina tax on Partner A’s \$1,000 of income.

Partner A is required to file an NC Tax Return. Partner A’s adjusted gross income includes the \$800 of business income from Taxed Partnership XYZ.<sup>18</sup> Partner A is required to add the \$200 for bonus depreciation on Partner A’s NC Tax Return. Partner A is allowed to deduct \$1,000 for the distributive share of income included in Taxed Partnership XYZ’s North Carolina taxable income.<sup>19</sup>

**B4. I am an Owner of a Taxed PTE. I have become aware that the Taxed PTE did not pay the full amount of tax shown due on the Taxed PTE’s NC Tax Return. How does that impact me as an Owner of the Taxed PTE?**

It depends. North Carolina law requires a Taxed PTE to pay the full amount of North Carolina tax it owes. If the Taxed PTE does not pay the full amount of tax it owes, the Department must collect the tax due from the PTE. However, if the PTE does not pay the full amount of tax due within 60 days of being notified of the outstanding liability, the Owner of the PTE is not eligible to take a deduction for the Owner’s distributive share of income from the PTE. The Department will send the Owner of the PTE a Notice of Proposed Assessment for the tax year disallowing the deduction for the Owner’s share of income from the PTE.<sup>20</sup>

**B5. I am an Owner of a Taxed PTE. I was allocated a net loss from the Taxed PTE for the tax year. How do I account for this loss on my NC Tax Return?**

When calculating North Carolina taxable income, a taxpayer that is an Owner of a Taxed PTE must add the amount of the taxpayer’s share of net loss from the Taxed PTE to the taxpayer’s federal adjusted gross income to the extent the net loss was included in the Taxed PTE’s North Carolina taxable income.<sup>21</sup>

**B6. Is a nonresident Owner of a Taxed PTE required to file an NC Tax Return?**

S Corporations

The North Carolina Administrative Code provides that “[a] nonresident shareholder in an S Corporation shall not be required to file a North Carolina individual income tax return when the only income from North Carolina sources is his or her share of S Corporation income and the S Corporation pays the tax on his or her behalf.”<sup>22</sup> This rule applies to nonresident shareholders of

<sup>18</sup> For individual income tax purposes, the starting point for determining North Carolina taxable income is adjusted gross income as defined in the Internal Revenue Code (“Code”) as of a certain date. See [N.C. Gen. Stat. §§ 105-153.4](#) and [105-228.90\(b\)\(7\)](#).

<sup>19</sup> See SB 105, s. 42.5.(i), [S.L. 2021-180](#).

<sup>20</sup> See SB 105, s. 42.5.(c,h), [S.L. 2021-180](#).

<sup>21</sup> See SB 105, s. 42.5.(i), [S.L. 2021-180](#).

<sup>22</sup> [17 NCAC 06B .4003\(c\)](#).



Taxed S Corporations to the extent the Taxed S Corporation complies with the provisions of new N.C. Gen. Stat. § 105-131.1A.<sup>23</sup>

### Partnerships

The North Carolina Administrative Code provides that “[a] nonresident individual partner is not required to file a North Carolina individual income tax return when the only income from North Carolina sources is the nonresident’s share of income from a partnership doing business in North Carolina, and the manager of the partnership has reported the income of the nonresident partner, including any guaranteed payments made to the partner, and paid the tax due.”<sup>24</sup> This rule applies to nonresident partners of Taxed Partnerships to the extent the Taxed Partnership complies with the provisions of new N.C. Gen. Stat. § 105-154.1.<sup>25</sup>

**Note:** If the Secretary believes that an individual is liable for North Carolina individual income tax, the Secretary may require the individual to file an NC Tax Return with the Department.<sup>26</sup>

## **Topic C: Owner of a Taxed PTE and North Carolina Income Tax Credits**

**C1. I am a North Carolina resident Owner of a Taxed PTE. Can I claim a tax credit for income taxes paid to another state by the Taxed PTE on my NC Tax Return?**

No. See the information outlined below.

### Taxed S Corporation

A Taxed S Corporation is allowed a tax credit against the income taxes levied against it by North Carolina so long as the Taxed S Corporation was subject to and paid income tax to another state or country on the same income that North Carolina taxed under new N.C. Gen. Stat. § 105-131.1A with respect to resident shareholders.<sup>27</sup>

The resident shareholder of a Taxed S Corporation is not allowed a tax credit on the shareholder’s NC Tax Return for taxes paid by the Taxed S Corporation to another state or country on income that is taxed to the Taxed S Corporation.<sup>28</sup>

### Taxed Partnership

A Taxed Partnership is allowed a tax credit against the income taxes levied against it by North Carolina so long as the Taxed Partnership was subject to and paid income tax to another state or country on income that was taxed to the Taxed Partnership with respect to its resident partners.

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<sup>23</sup> See SB 105, s. 42.5.(c), [S.L. 2021-180](#).

<sup>24</sup> [NCAC 06B .3513\(c\)](#).

<sup>25</sup> See SB 105, s. 42.5.(h), [S.L. 2021-180](#).

<sup>26</sup> [N.C. Gen. Stat. § 105-153.8\(a\)\(3\)](#)

<sup>27</sup> See SB 105, s. 42.5.(j), [S.L. 2021-180](#).

<sup>28</sup> See SB 105, s. 42.5.(j), [S.L. 2021-180](#).

The resident partner of a Taxed Partnership is not allowed a tax credit on the individual's NC Tax Return for taxes paid by the Taxed Partnership to another state or country on income that is taxed to the Taxed Partnership.<sup>29</sup>

**C2. I am a North Carolina resident Owner of a Taxed PTE. The Taxed PTE does business in North Carolina and State XYZ. State XYZ does not allow the PTE to pay income tax at the entity level. As an Owner, I filed an income tax return in State XYZ and paid income tax to that state. Can I claim the tax credit for income taxes paid to State XYZ on my NC Tax Return?**

It depends. A PTE may be a Taxed PTE for North Carolina tax purposes, but may not be a taxed entity in another state. In such cases, the other state's income tax, if any, is paid by the Owner(s) of the PTE.

If a Taxed PTE for North Carolina purposes is not a taxed entity in another state where the PTE does business and the Owner of the PTE pays income tax to the other state on their share of income from the PTE, the North Carolina resident Owner of the PTE may be allowed a tax credit for income taxes paid to other states subject to the provisions of new N.C. Gen. Stat. § 105-153.9(a)(4) (for Taxed S Corporation shareholders) or new N.C. Gen. Stat. § 105-153.9(a)(5) (for Taxed Partnership partners).<sup>30</sup>

These statutory provisions instruct the Owners of a Taxed PTE to use their share of the income from the Taxed PTE and the amount of tax imposed on the Taxed PTE when calculating their North Carolina income tax credit.

**C3. I am a North Carolina resident Owner of a PTE. The PTE did not make the Taxed PTE election. The PTE does business in North Carolina and State XYZ. The PTE filed an income tax return and paid income tax in State XYZ. Can I claim the tax credit for income taxes paid to another state by the PTE on my NC Tax Return?**

In some instances, a PTE that is not a Taxed PTE for North Carolina tax purposes may elect or be required to pay income tax as an entity under the laws of another state. In such circumstances, North Carolina does not provide a mechanism for the PTE to claim a North Carolina tax credit for income taxes the PTE paid to the other state. If allowable at all, the tax credit must be taken by the resident Owner of the PTE on their NC Tax Return. The Owner's eligibility for the tax credit is dependent on the type of PTE as outlined below.

S Corporation

[N.C. Gen. Stat. § 105-131.8\(a\)](#) provides that, “[f]or purposes of [N.C. Gen. Stat. §§ 105-153.9](#) and [105-160.4](#), each resident shareholder is considered to have paid a tax imposed on the shareholder in an amount equal to the shareholder's pro rata share of any net income tax paid by the S Corporation to a state that does not measure the income of S Corporation shareholders by the income of the S Corporation. For purposes of the preceding sentence, the term “net income tax” means any tax imposed on or measured by a corporation's net income.”

**Note:** In order to qualify for the tax credit, the other state cannot have measured the income of the North Carolina resident shareholders by the income of the S Corporation. For taxes paid by

<sup>29</sup> See SB 105, s. 42.5.(j), [S.L. 2021-180](#).

<sup>30</sup> See SB 105, s. 42.5.(j), [S.L. 2021-180](#).

an S Corporation to a state that imposes a tax on the S Corporation that meets the requirements of [N.C. Gen. Stat. § 105-131.8\(a\)](#), the North Carolina resident shareholder can claim a tax credit for taxes paid to the other state subject to the provisions of [N.C. Gen. Stat. §§ 105-153.9](#) and [105-160.4](#). For taxes paid by an S Corporation to a state that imposes a tax on the S Corporation that does not meet the requirements of [N.C. Gen. Stat. § 105-131.8\(a\)](#) the North Carolina resident shareholders cannot claim a tax credit for taxes paid to that state.

For guidance on the impact of another state's tax laws on your specific situation, you may request written advice under the provisions of the Department's [Written Determination Policy](#).

### Partnership

There is no provision in North Carolina law that allows a North Carolina resident partner of a partnership to claim a tax credit for entity-level income taxes paid by the partnership to another state. Consequently, any income tax required to be paid (or elected to be paid) to another state by a partnership as an entity under the laws of the other state cannot be claimed by the North Carolina resident partner as a tax credit on the partner's NC Tax Return.

## **C4. I am an Owner of a Taxed PTE. Are there any special rules on who can claim a North Carolina income tax credit?**

### General Rule

A Taxed PTE that qualifies to claim an income tax credit may apply each Owner's share of the tax credit against the Owner's share of the Taxed PTE's income tax.

A Taxed PTE cannot pass a North Carolina income tax credit to its Owners. In addition, a PTE cannot pass to its Owners any carryforward of an unused portion of a tax credit that was claimed by the Taxed PTE on the Taxed PTE's NC Tax Return.

### Income Tax Credits Required to be Taken in Installments

A Taxed PTE must pass through to its Owners any income tax credit required to be taken in installments if the first installment of the tax credit was claimed by the Owner of the Taxed PTE. In addition, a Taxed PTE must pass through to its Owners any carryforward of an unused income tax credit required to be taken in installments if the first installment of the tax credit was claimed by the Owner of the Taxed PTE.

A Taxed PTE cannot pass through to its Owners any income tax credit required to be taken in installment if the first installment of the tax credit was claimed by the Taxed PTE. In addition, a Taxed PTE cannot pass through to its Owners any carryforward of an unused income tax credit required to be taken in installments if the first installment of the tax credit was claimed by the Taxed PTE.

## **Assistance**

If you have any questions about this notice, you may call the North Carolina Department of Revenue Customer Interaction Center at 1-877-252-3052 (8:00 am until 4:30 pm EST, Monday through Friday), or write the Department at PO Box 25000, Raleigh, NC 27640-0640.

*To the extent there is any change to a statute or regulation, or new case law subsequent to the date of this notice, the provisions in this notice may be superseded or voided. To the extent that any provisions in any other notice, directive, technical bulletin, or published guidance regarding the subject of this notice and issued prior to this notice conflict with this notice, the provisions contained in this important notice supersede the previous guidance.*