2005 DRAFTING REQUEST

Bill

Received: **09/27/2004**

Received By: **jkreye**

Wanted: **As time permits**

Identical to LRB:

For: **Administration-Budget**

By/Representing: **Justus**

This file may be shown to any legislator: **NO**

Drafter: **jkreye**

May Contact:

Addl. Drafters:

Subject: **Tax, Individual - income**
Tax, Business - crp inc, fran

Extra Copies:

Submit via email: **NO**

Pre Topic:

DOA:......Justus, BB0068 -

Topic:

Require withholding from nonresident members of pass-through entities

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Instructions:

See Attached

Drafting History:

Vers.	Drafted	Reviewed	Typed	Proofed	Submitted	Jacketed	Required
/?	jkreye 09/28/2004	wjackson 10/15/2004 wjackson 10/19/2004		_______ _______ _______ _______			State
/1	jkreye 11/04/2004	wjackson 11/04/2004	pgreensl 10/19/2004	_______ _______	sbasford 10/19/2004		State
/2			rschluet 11/05/2004	_______ _______	sbasford 11/05/2004		

FE Sent For:

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BB0068

2003-05 Budget Bill Statutory Language Drafting Request

- Topic: Require withholding from nonresident members of pass-through entities
- Tracking Code: (Assigned by Government Operations Team)
- SBO team: Tax & Justice
- SBO analyst: Sarah Justus
  - Phone: 7-6921
  - Email: sarah.justus@doa.state.wi.us
- Agency acronym: DOR
- Agency number: 566

0306

Statutory Language Request
Wisconsin Department of Revenue

TITLE: REQUIRE WITHHOLDING FROM NONRESIDENT MEMBERS OF PASS-THROUGH ENTITIES

DESCRIPTION OF CURRENT LAW AND PROBLEM

Under current law, partnerships, including limited liability companies treated as partnerships, are not subject to Wisconsin franchise or income tax. Instead their partners or members are required to file Wisconsin franchise or income tax returns and pay tax on their share of the income allocable to services performed, business transacted, or property located in Wisconsin.

Shareholders of tax-option (S) corporations are subject to Wisconsin income tax on their share of the corporation's Wisconsin income. If a shareholder does not file a Wisconsin return and pay the Wisconsin tax due on his or her share of tax-option (S) corporation income, the corporation may be taxed on that shareholder's share of the corporation's Wisconsin income. However, the statute of limitations for both the corporation and the shareholder may expire before the department determines that a shareholder did not pay the tax due on the share of tax-option (S) corporation income and, as a result, the corporation's income is never subject to tax.

Between 1996 and 2003, Wisconsin experienced over a 213% increase in the number of pass-through entities, not counting general partnerships. This increase is primarily due to the creation of limited liability companies and registered limited liability partnerships and the easing of requirements for tax-option (S) corporations. More pass-through entities than regular corporations are now doing business in Wisconsin [see Attachment 2]. Many of these pass-through entities have nonresidents as owners. It is unknown how many nonresident owners actually file required Wisconsin income tax returns.

Nonresident beneficiaries of estates and trusts may also be subject to Wisconsin taxation. Based on a sample of returns, it appears that many nonresident beneficiaries are not filing required Wisconsin income tax returns either.

To ensure that nonresident owners are paying their fair share of state income taxes, the Multistate Tax Commission has recommended a Model S Corporation Income Tax Act [see Attachment 3] and Proposed Statutory Language on Reporting Options for Non-resident Members of Pass-through Entities with Withholding Requirement [see Attachment 4]. Approximately 30 states have adopted withholding provisions for some or all nonresident owners [see Attachment 5].

RECOMMENDATION FOR ACTION

To encourage compliance with Wisconsin franchise and income tax laws, pass-through entities should be required to withhold Wisconsin income tax from their nonresident owners.

ADMINISTRATIVE IMPACT

This proposal would facilitate the collection of Wisconsin income taxes owed by nonresidents who own interests in pass-through entities that do business in Wisconsin.

FAIRNESS /TAX EQUITY

Since nonresidents who are employees or lottery prize winners currently are subject to Wisconsin withholding, those nonresidents who derive income from pass-through entities should also be subject to withholding.

IMPACT ON ECONOMIC DEVELOPMENT

None.

FISCAL EFFECT

FY06: +$7.5 million; FY07: +$5.0 million.

DRAFTING INSTRUCTIONS

See Attachment 1.

EFFECTIVE DATE AND/OR INITIAL APPLICABILITY

Taxable years of pass-through entities that begin on January 1, 2005.

INTERESTED/AFFECTED PARTIES

Pass-through entities; attorneys and tax accountants

DOR CONTACT PERSON

Diane Hardt
266-6798
dhardt@dor.state.wi.us

PREPARED BY Carol Held

Subch. XII ? or 71.775

610.

Attachment 1 — Drafting Instructions

Amend the Wisconsin Statutes to provide the following:

1. For the privilege of doing business in the state or deriving income from property located in the state, a partnership, limited liability company, tax-option corporation, estate, or trust that is treated as a pass-through entity for federal income tax purposes and that has Wisconsin income for the taxable year which is allocable to a nonresident partner, nonresident shareholder, or nonresident beneficiary shall pay a withholding tax.

definition

2. A nonresident includes an individual who is not domiciled in the state; a partnership, limited liability company, or corporation whose commercial domicile is outside the state; and an estate or trust that is a nonresident under secs. 71.14 (1) through (3m).

3. The amount of withholding shall be equal to the partner's, member's, shareholder's, or beneficiary's share of income attributable to Wisconsin multiplied by:

   a. The highest tax rate for a single individual for the taxable year under sec. 71.06, if the recipient is an individual, estate, or trust, or
   b. The highest tax rate for the taxable year under sec. 71.27 for a partnership, limited liability company, corporation, or tax-option corporation.

4. ~~Withholding will not be required in the following situations~~: The following are not subject to the withholding tax under this section.

   a. If the person is exempt from taxation under ch. 71. The pass-through entity may rely on a written statement of the person claiming to be exempt from the tax provided the pass-through entity attaches a copy of the statement to its return for the current taxable year. The statement must disclose the complete name, address, federal employer identification number, and reason for the exemption for each person who claims to be exempt from tax.
   b. If the pass-through entity is a joint venture that has elected not to be treated as a partnership under section 761 of the Internal Revenue Code for federal income tax purposes.
   c. If the person has no other source of Wisconsin income and the person's share of income from the pass-through entity is less than $1,000.

5. A member of a pass-through entity that is itself a pass-through entity shall be subject to the same requirement to withhold and pay tax on the share of income distributable to each of its nonresident members.

6. Each partnership, limited liability company, tax-option corporation, estate, or trust that is required to withhold tax shall pay the amount withheld to the department no later than:

   a. Tax-option corporations: the 15th day of the 3rd month following the close of the taxable year.
   b. Partnerships and limited liability companies: the 15th day of the 4th month following the close of the taxable year.
   c. Estates and trusts: the 15th day of the 4th month following the close of the taxable year.

7. If the pass-through entity has an extension of time to file, the withholding is still due on the unextended due date of the entity's return as provided under sec. 71.24(1), 71.20(1), or 71.13(1), Wis. Stats. As long as 90% of the withholding tax due for the current taxable year, or 100% of the withholding tax due for the prior taxable year if that taxable year was a period of 12 months and the entity paid withholding tax as provided under this section, is paid by the unextended due date, no underpayment of estimated tax under sec. 71.09 or 71.29 will be imposed. However, interest at 12% will be imposed on the unpaid withholding during the extension period. Interest at 18% will be imposed for the period from the extended due date until the date the payment is made.

8. The pass-through entity shall annually notify each nonresident person of the Wisconsin withholding paid on the person's behalf on or before the extended due date of the pass-through entity's return. The pass-through entity shall furnish a copy of the notice to the department with the return that it files for the taxable year.

9. The person may claim credit for the amount withheld on the person's own Wisconsin income or franchise tax return. The withholding is considered to be paid on the last day of the pass-through entity's taxable year for which the tax was paid.

10. Any tax withheld shall be held in trust for the state. The pass-through entity shall be liable to the department for the payment of the tax required to be withheld under this section. No partner, member, shareholder, or beneficiary shall have a right of action against the pass-through entity in respect to any amount withheld and paid over in compliance with this section.

11. If a pass-through entity fails to withhold tax as required by this section, the pass-through entity shall be liable for any tax, interest, and penalties. If the nonresident partner, member, shareholder, or beneficiary files a return and pays the tax due, the pass-through entity will not be liable for the tax. However, the pass-through entity will continue to be liable for any interest or penalties otherwise applicable for failure to withhold under secs. 71.82(d) and 71.83.

(2)

Types of Entities

Entity	12/31/96	12/31/97	12/31/98	11/31/99	12/31/00	12/31/01	12/31/02	12/31/03
Corporations								
New	10,119	9,762	8,920	8,517	8,428	7,359	7,364	7,171
Total	107,008	113,274	117,954	122,276	126,460	129,528	132,815	135,949
S corporations	37,000	40,000	42,000	45,000	48,000	51,000	54,000	56,000
Limited Partnerships (LPs)								
New	415	488	391	356	429	345	340	256
Total	4,852	5,258	5,495	5,807	6,142	6,393	6,635	6,784
Limited Liability Companies (LLCs)								
New	4,124	6,149	8,136	10,298	12,295	14,582	18,192	22,229
Total	9,762	15,646	22,640	33,123	44,715	58,642	76,502	97,068
Limited Liability Partnerships (LLPs)								
New	891	973	809	605	498	440	375	355
Total	900	1,825	2,050	3,171	3,659	4,036	4,367	4,648
Total Pass-Through Entities								
	52,514	62,729	72,185	87,101	102,516	120,071	141,504	164,500
Total C Corporations								
	70,008	73,274	75,954	77,276	78,460	78,528	78,815	79,949

Note: Information for 1996 through 2003, except about S corporations, is from the Department of Financial Institutions. The S corporation figures are Department of Revenue estimates.

Attachment 3

American Bar Association Section of Taxation
Committee on S Corporations
Subcommittee on the State Taxation of S Corporations
June 1989 (Revised)

Model S Corporation Income Tax Act

Recommended (with Six Proposed Modifications) to the States
by the Multistate Tax Commission, August 2, 1991

I. BASIC PROVISIONS

SECTION 1000. TITLE; DEFINITIONS; FEDERAL CONFORMITY; CONSTRUCTION

(a) The title of this Part shall be the [name of State] S Corporation Income Tax Act.

(b) For purposes of this Part, the following terms shall have the following meanings:

(1) C Corporation: a corporation which is not an S Corporation.

(2) Code: the Internal Revenue Code of 1986, as amended and as applicable to the Taxable Period; references to sections of the Code shall be deemed to refer to corresponding provisions of prior and subsequent federal tax laws.

(3) Income Attributable to the State: items of income, loss, deduction or credit of the S Corporation apportioned to this State pursuant to [Section number—business income apportionment provision] or allocated to this State pursuant to [Section number—nonbusiness income allocation provision].

(4) Income Not Attributable to the State: all items of income, loss, deduction or credit of the S Corporation other than Income Attributable to the State.

(5) Post–Termination Transition Period: that period defined in Section 1377(b)(1) of the Code.

(6) Pro Rata Share: the portion of any item attributable to an S Corporation shareholder for a Taxable Period determined in the manner provided in, and subject to any election made under, Section 1377(a) or 1362(e), as the case may be, of the Code.

(7) S Corporation: a corporation for which a valid election under Section 1362(a) of the Code is in effect.

(8) Taxable Period: any taxable year or portion of a taxable year during which a corporation is an S Corporation.

(c) Except as otherwise expressly provided or clearly appearing from the context, any term used in this Part shall have the same meaning as when used in a comparable context in the Code, or in any statute relating to federal income taxes, in effect for the Taxable Period. Due consideration shall be given in the interpretation of this Part to applicable sections of the Code in effect from time to time and to federal rulings and regulations interpreting such sections, provided such Code, rulings and regulations do not conflict with the provisions of this Part.

(d) This Act shall be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject matter of this Act among States enacting it.

SECTION 1001. TAXATION OF AN S CORPORATION AND ITS SHAREHOLDERS

(a) [Alternative No. 1] An S Corporation shall not be subject to the tax imposed by [Section number—taxation of C Corporations].

(a) [Alternative No. 2] Except as provided in the following sentence, an S Corporation shall not be subject to the tax imposed by [Section number—taxation of C Corporations]. If an S Corporation is subject to federal income tax on any of its income, then the amount of such income, as modified pursuant to Section 1002 of this Part, that constitutes Income Attributable to the State shall be subject to the tax imposed by [Section number—taxation of C Corporations]. The S Corporations Income Attributable to the State shall be reduced by the amount of any tax imposed on the corporation pursuant to the preceding sentence.

(b) For purposes of [Section number—taxation of individuals], each shareholder's Pro Rata Share of the S Corporation's Income Attributable to the State and each resident shareholder's Pro Rata Share of the S Corporation's Income Not Attributable to the State, as modified pursuant to Section 1002 of this Part, shall be taken into account by the shareholder in the manner provided in Section 1366 of the Code.

(c) For purposes of determining the amounts taken into account by the shareholders of an S Corporation pursuant to subsection (b), the amount of any tax imposed on the S Corporation under the Code shall proportionately reduce the S Corporation's Income Attributable to the State and Income Not Attributable to the State.

SECTION 1002. MODIFICATION AND CHARACTERIZATION OF INCOME

(a) An S Corporation's Income Attributable to the State shall, for purposes of Section 1001 of this Part, be subject to the modifications provided in [Section number—corporate modifications].

(b) The Pro Rata Share of each resident shareholder of an S Corporation in the Income Not Attributable to the State shall, for purposes of Section 1001(b) of this Part, be subject to the modifications provided in [Section number—individual modifications].

(c) The character of any S Corporation item taken into account by a shareholder of an S Corporation pursuant to Section 1001(b) of this Part shall be determined as if such item were received or incurred by the S Corporation and not its shareholder.

SECTION 1003. BASIS AND ADJUSTMENTS

(a) The initial basis in the hands of a resident shareholder of an S Corporation in the stock of the S Corporation and any indebtedness of the S Corporation to the shareholder shall be determined in the manner provided under the Code, and shall be determined as of the date (which may be before the effective date of this Part) that is the latest to occur of (1) the date on which the shareholder last became a resident of this State, (2) the date on which the shareholder acquired the stock or the indebtedness of the corporation, or (3) the effective date of the corporation's most recent S election under the Code.

(b) The initial basis of a resident shareholder in the stock and indebtedness of an S Corporation shall be adjusted after the date specified in subsection (a) in the manner and to the extent required by Section 1011 of the Code except that, with respect to any Taxable Period during which the shareholder is a resident of this State—

(1) any modifications made (other than for income exempt from federal or this State's taxation) pursuant to Section 1002 of this Part [(and any provision of prior State law similar to this subsection (b), without regard to subsection (b)(2))] shall be taken into account; and

(2) any adjustments made pursuant to Section 1367 of the Code for a Taxable Period during which this State did not measure the income of a shareholder of an S Corporation by reference to the S Corporation's income shall not be taken into account.

(c) The initial basis in the hands of a nonresident shareholder of an S Corporation in the stock of the S Corporation and any indebtedness of the S Corporation to the shareholder shall be zero as of the date (which may be before the effective date of this Part) that is the latest to occur of (1) the date on which the shareholder last became a nonresident of this State, (2) the date on which the shareholder acquired the stock or the indebtedness of the corporation, or (3) the effective date of the corporation's most recent S election under the Code.

(d) The initial basis of a nonresident shareholder in the stock and indebtedness of an S Corporation shall be adjusted after the date specified in subsection (c) as provided in Section 1367 of the Code, except that such adjustments shall be limited to that portion of the Income Attributable to the State that is taken into account by the shareholder pursuant to Section 1001(b) of this Part [(and any provision of prior State law similar to this subsection (d))]. In computing

Income Attributable to the State for purposes of the preceding sentence, any modification made for income exempt from federal or this State's taxation shall not be taken into account.

(e) The basis in the hands of a resident shareholder of an S Corporation in the stock of the S Corporation shall be reduced by the amount allowed as a loss or deduction pursuant to Section 1004(d) of this Part.

(f) The basis in the hands of a resident shareholder of an S Corporation in the stock of the S Corporation shall be reduced by the amount of any cash distribution which is not taxable to the shareholder as a result of the application of Section 1006(b) of this Part.

(g) For purposes of this section, any person acquiring stock or indebtedness of an S Corporation by gift from a person who is a resident of this State at the time of the gift shall be considered to have acquired the stock or indebtedness at the time the donor acquired the stock or indebtedness.

SECTION 1004. CARRYOVERS AND CARRYBACKS; LOSS LIMITATION

(a) Carryforwards and carrybacks to and from Taxable Periods of an S Corporation shall be restricted in the manner provided in Section 1371(b) of the Code.

(b) The aggregate amount of losses or deductions of an S Corporation taken into account by a shareholder of the S Corporation for a Taxable Period pursuant to Section 1001(b) of this Part shall not exceed the shareholder's combined adjusted basis, determined in accordance with Section 1003 of this Part, in the stock of the S Corporation and any indebtedness of the S Corporation to the shareholder.

(c) Any loss or deduction of an S Corporation which is disallowed for a Taxable Period pursuant to subsection (b) shall be treated as incurred by the corporation in the succeeding Taxable Period with respect to that shareholder.

(d) (1) Any loss or deduction of an S Corporation which is disallowed pursuant to subsection (b) for the corporation's last Taxable Period as an S Corporation shall be treated as incurred by a shareholder on the last day of any Post-Termination Transition Period.

(2) The aggregate amount of losses and deductions taken into account by a shareholder pursuant to subsection (d)(l) shall not exceed the shareholder's adjusted basis in the stock of the corporation (determined in accordance with Section 1003 of this Part at the close of the last day of any Post-Termination Transition Period and without regard to this subsection (d)).

(e)[Optional subsection] Any loss or deduction of an S Corporation for a Taxable Period that is not taken into account by a shareholder of the S Corporation pursuant to [Section numbers—at-risk, passive loss, etc. limitations] shall be treated as incurred by the corporation in the succeeding Taxable Period with respect to that shareholder.

SECTION 1005. PART-YEAR RESIDENCE

For purposes of this Part, if a shareholder of an S Corporation is both a resident and nonresident of this State during any Taxable Period, the shareholder's Pro Rata Share of the S Corporation's Income Attributable to the State and Income Not Attributable to the State for the Taxable Period shall be further prorated between the shareholder's periods of residence and nonresidence during the Taxable Period, in accordance with the number of days in each period.

SECTION 1006. DISTRIBUTIONS

(a) Subject to subsection (c), a distribution made by an S Corporation with respect to its stock to a resident shareholder shall be taken into account by the shareholder for purposes of [Section number—taxation of individuals] to the extent that the distribution is treated as a dividend or as gain from the sale or exchange of property pursuant to Section 1368 of the Code.

(b) Subject to subsection (c), a distribution of money made by a corporation with respect to its stock to a resident shareholder during a Post-Termination Transition Period shall not be taken into account by the shareholder for purposes of [Section number—taxation of individuals] to the extent the distribution is applied against and reduces the adjusted basis of the stock of the shareholder in accordance with Section 1371(e) of the Code.

(c) In applying Sections 1368 and 1371(e) of the Code to any distribution referred to in subsection (a) or (b)—

(1) the term "adjusted basis of the stock" shall mean the shareholder's adjusted basis in the stock of the S Corporation, as determined under Section 1003 of this Part; and

(2) the term "accumulated adjustments account" shall mean an amount that is equal to, and adjusted in the same manner as, the S Corporation's accumulated adjustments account defined in Section 1368(e)(1)(A) of the Code, except that any modifications required to be made pursuant to Section 1002(a) of this Part shall be taken into account.

SECTION 1007. RETURNS; SHAREHOLDER AGREEMENTS; MANDATORY PAYMENTS

(a) An S Corporation which engages in activities in this State which would subject a C Corporation to the requirement to file a return under [Section number—taxation of C Corporations] shall file with the [State taxing authority] an annual return, in the form prescribed by the [State taxing authority], on or before the due date prescribed for the filing of C Corporation returns under [Section number—corporate tax return filing date]. The return shall set forth the name, address and social security or federal identification number of each shareholder; the Income Attributable to the State and Income Not Attributable to the State with respect to each shareholder as determined under this Part; the modifications required by Section 1002 of this Part; and such other information as the [State taxing authority] may by regulation prescribe. The S Corporation shall, on or before the day on which such return is filed, furnish to each person who was a shareholder during the year a copy of such information shown on the return as the [State taxing authority] may by regulation prescribe. The S Corporation shall also maintain the accumulated adjustments account described in Section 1006(c)(2) of this Part.

(b) The [State taxing authority] shall permit S Corporations to file composite returns and to make composite payments of tax on behalf of some or all of its nonresident shareholders. The [State taxing authority] may permit composite returns and payments to be made on behalf of resident shareholders.

(c) With respect to each of its nonresident shareholders, an S Corporation shall for each Taxable Period either (1) timely file with the [State taxing authority] an agreement as provided in subsection (d) or (2) make a payment to this State as provided in subsection (e). An S Corporation that timely files an agreement as provided in subsection(d) with respect to a nonresident shareholder for a Taxable Period shall be considered to have timely filed such an agreement for each subsequent Taxable Period. An S Corporation that does not timely file such an agreement for a Taxable Period shall not be precluded from timely filing such an agreement for subsequent Taxable Periods.

(d) The agreement referred to in subsection (c)(1) is an agreement of a non-resident shareholder of the S Corporation—

(1) to file a return in accordance with the provisions of [Section number—individual tax return filing requirement] and to make timely payment of all taxes imposed on the shareholder by this State with respect to the income of the S Corporation; and

(2) to be subject to personal jurisdiction in this State for purposes of the collection of income taxes, together with related interest and penalties, imposed on the shareholder by this State with respect to the income of the S Corporation.

The agreement will be considered to be timely filed for a Taxable Period (and for all subsequent Taxable Periods) if it is filed at or before the time the annual return for such Taxable Period is required to be filed pursuant to subsection (a).

(e)The payment referred to in subsection (c)(2) shall be in an amount equal to the highest marginal tax rate in effect under [Section number—individual tax rates] multiplied by the shareholder's Pro Rata Share of the Income Attributable to the State reflected on the corporation's return for the Taxable Period. An S Corporation shall be entitled to recover a payment made pursuant to the preceding sentence from the shareholder on whose behalf the payment was made. Any such payment for a Taxable Period must be made at or before the time the annual return for such Taxable Period is required to be filed pursuant to subsection (a).

(f) Any amount paid by the corporation to this State pursuant to subsection (b) or (e) shall be considered to be a payment by the shareholder on account of the income tax imposed on the shareholder for the Taxable Period pursuant to [Section number—taxation of individuals].

SECTION 1008. TAX CREDITS

(a) For purposes of [Section number—individual tax credit allowance provisions], each resident shareholder shall be 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 which does not measure the income of shareholders of an S Corporation by reference to 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.

(b) [Optional] Each shareholder of an S Corporation shall be allowed a credit against the tax imposed by [Section number—taxation of individuals] in an amount equal to the shareholder's Pro Rata Share of the tax credits described in [Section number—policy tax credits available to a C Corporation].

II. ADDENDUM: CONFORMING PROVISIONS

A. LIFO RECAPTURE (OPTIONAL)

If a corporation is subject to LIFO recapture pursuant to Section 1363(d) of the Code, then—

(1) any increase in the tax imposed by [Section number—taxation of C Corporations] by reason of the inclusion of the LIFO recapture amount in its income shall be payable in four equal installments;

(2) the first installment shall be paid on or before the due date (determined without regard to extensions) for filing the return for the first taxable year for which the corporation was subject to the LIFO recapture;

(3) the three succeeding installments shall be paid on or before the due date (determined without regard to extensions) for filing the corporation's return for the three succeeding taxable years; and

(4) for purposes of computing interest on underpayments, the last three installments shall not be considered underpayments until after the payment due date specified above.

B. SAMPLE INDIVIDUAL INCOME TAX PROVISION

[To be inserted in the section determining State taxable income of individuals]

Notwithstanding any other provision of this statute [or other statute designation], a shareholder of an S Corporation (as defined in Section 1000(b)(7)) shall take into account the income, loss, deduction or credit of the S Corporation only to the extent provided in Section 1001(b).

C. SAMPLE CORPORATE INCOME TAX PROVISIONS

[Alternative A—to be inserted in the section determining State taxable income of corporations when an S Corporation is never subject to income tax]

Notwithstanding any other provision of this statute [or other statute designation], an S Corporation (as defined in Section 1000(b)(7)) shall not be subject to the income tax imposed under this section.

[Alternative B—to be inserted in the section determining State taxable income of corporations when an S Corporation will be subject to income tax]

Notwithstanding any other provision of this statute [or other statute designation], an S Corporation (as defined in Section 1000(b)(7)) shall be taxed on its income only to the extent provided in Section 1001(a).

Six Proposed Modifications to The American Bar Association Model S Corporation Income Tax Act

[Note that the Six Proposed Modifications contained in this document have been developed to suggest amendatory language to states considering the American Bar Association Model S Corporation Income Tax Act that would be consistent with* existing *state tax policy. In this sense, an adopting state is not encouraged to adopt any of the Six Proposed Modifications unless the modification being considered is consistent with* existing *state tax policy of the state and the adopting state wishes to preserve the* existing *policy choice represented by one or more of the Six Proposed Modifications.]

PROPOSED MODIFICATION #1

(Accommodating state restrictions against incorporation of the Internal Revenue Code *in futuro*)

Original Draft: Section 1000(b)(2)--

Code: the Internal Revenue Code of 1986, as amended and as applicable to the Taxable Period; reference to sections of the Code shall be deemed to refer to corresponding provisions of prior and subsequent federal tax laws.

Original Draft: Section 1000(c)--

Except as otherwise expressly provided or clearly appearing from the context, any term used in this Part shall have the same meaning as when used in a comparable context in the Code, or in any statute relating to federal income taxes, in effect for the Taxable Period. Due consideration shall be given in the interpretation of this Part to applicable sections of the Code in effect from time to time and to federal rulings and regulations interpreting such sections, provided such Code, rulings and regulations do not conflict with the provisions of this Part.

Optional Draft: Section 1000(b)(2) [MTC Alternative]--

Code: the Internal Revenue Code of 1986, as amended and as applicable to the Taxable Period pursuant to [Section number--state provision conforming state tax laws to the Internal Revenue Code as of a specified date including to the extent noted provisions amended, deleted, or added thereto prior to the applicable effective date].

Optional Draft: Section 1000(c) [MTC Alternative]--

Except as otherwise expressly provided in this Part or other applicable law or clearly appearing from the context, any term used in this Part shall have the same meaning as when used in a comparable context in the Code, or in any statute relating to federal income taxes, in effect for the Taxable Period pursuant to [Section number--state provision conforming state tax laws to the Internal Revenue Code as of a specified date including to the extent noted provisions amended, deleted, or added thereto prior to the applicable effective date]. Due consideration shall be given in the interpretation of this Part to analogous sections of the Code and to federal rulings and regulations interpreting such sections, provided such Code, rulings and regulations do not conflict with the provisions of this Part.

PROPOSED MODIFICATION #2

(Permitting entity level taxation by states in addition to the taxation of federal built-in gains and excessive passive net income)

Original Draft: Section 1001(a) [Alternative No. 2]--

Except as provided in the following sentence, an S Corporation shall not be subject to the tax imposed by [Section number--taxation of C corporations]. If an S Corporation is subject to federal income tax on any of its income, then the amount of such income, as modified pursuant to Section 1002 of this Part, that constitutes Income Attributable to the State shall be subject to the tax imposed by [Section number--taxation of C corporations]. The S Corporations Income Attributable to the State shall be reduced by the amount of any tax imposed on the corporation pursuant to the preceding sentence.

Optional Draft A: Section 1001(a) [MTC Alternative A] --

An S Corporation's Income Attributable to the State shall be subject to the tax imposed by [Section number--special tax on the income of S Corporations] and, for purposes of determining the amounts taken into account by the shareholder of an S Corporation pursuant to subsection (b), the amount of the tax shall reduce the S Corporation's Income Attributable to the State. An S corporation shall not be subject to the tax imposed by [Section number--taxation of C Corporations].

Optional Draft B: Section 1001(a) [MTC Alternative B]--

An S Corporation shall not be subject to the tax imposed by [Section number--taxation of C Corporations], except:

(1) If an S Corporation is subject to federal income tax on any of its income, then the amount of such income, as modified pursuant to Section 1002 of this Part, that constitutes Income Attributable to the State shall be subject to the tax imposed by [Section number--taxation of C Corporations].

(2) An S Corporation's Income Attributable to the State, less the amount of income subject to the tax imposed under paragraph (1) of this subsection, shall be subject to the tax imposed by [Section number--special tax on income of S Corporations].

For purposes of determining the amounts taken into account by the shareholders of an S Corporation pursuant to subsection (b), the amount of any tax imposed pursuant to this subsection shall reduce the S Corporation's Income Attributable to the State.

PROPOSED MODIFICATION #3

(Providing for an alternative which denies resident shareholder credit for entity-level tax imposed by non-recognition state)

Original Draft: Section 1008(a)--

For purposes of [Section number--individual tax credit allowance provisions], each resident shareholder shall be 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 which does not measure the income of shareholders of an S Corporation by reference to 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.

Optional Draft: Section 1008(a) [MTC Alternative]--

For purposes of [Section number--individual tax credit allowance provisions], a net income tax imposed on an S Corporation by another state shall not be creditable against the shareholder's tax liability.

PROPOSED MODIFICATION #4

(Providing for an alternative that prevents an automatic deduction of another state's income taxes by reason of the operation of IRC § 164)

Original Draft: Section 1002(b)--

The Pro Rata Share of each resident shareholder of an S Corporation in the Income Not Attributable to the State shall, for purposes of Section 1001(b) of this Part, be subject to the modifications provided in [Section number--individual modifications].

Optional Draft: Section 1002(b) [MTC Alternative]--

The Pro Rata Share of each resident shareholder of an S Corporation in the Income Not Attributable to the State shall, for purposes of Section 1001(b) of this Part, be--

(1) subject to the modifications provided in [Section number--individual modifications]; and

(2) increased by the amount of the shareholder's Pro Rata Share of any income tax imposed on the corporation by another state.

PROPOSED MODIFICATION #5

(Alternative provision which prohibits reduction of state taxable income passed through to the shareholders for federal Code Section 1374 and 1375 taxes imposed on the corporation.)

Original Draft: Section 1001(c)--

For purposes of determining the amounts taken into account by the shareholders of an S Corporation pursuant to subsection (b), the amount of any tax imposed on the S Corporation under the Code shall proportionately reduce the S Corporation's Income Attributable to the State and Income Not Attributable to a State.

Optional Draft: Section 1001(c) [MTC Alternative]--

For purposes of determining the amounts taken into account by the shareholders of an S Corporation pursuant to subsection (b), the amount of any tax imposed on the S Corporation under the Code shall not reduce the S Corporation's Income Attributable to the State and Income Not Attributable to a State.

PROPOSED MODIFICATION #6

(Optional provision requiring informational return to be filed by S Corporation in states where it has resident shareholders even though S Corporation does not operate within such state)

Original Draft: Section 1007(a)--

An S Corporation which engages in activities in this State which would subject a C Corporation to the requirement to file a return under [Section number--taxation of C Corporation] shall file with the [State taxing authority] an annual return, in the form prescribed by the [State taxing authority], on or before the due date prescribed for the filing of C Corporation returns under [Section number--corporate tax return filing date]. The return shall set forth the name, address and social security or federal identification number of each shareholder; the Income Attributable to the State and Income Not Attributable to the State with respect to each shareholder as determined under this Part; the modifications required by Section 1002 of this Part; and such other information as the [State taxing authority] may by regulations prescribe. The S Corporation shall, on or before the day on which such return is filed, furnish to each person who was a shareholder during the year a copy of such information shown on the return as the [State taxing authority] may by regulation prescribe. The S Corporation shall also maintain the accumulated adjustments account described in Section 1006(c)(2) of this Part.

Optional Draft: Section 1007(a) [MTC Alternative]--

Every S Corporation which engages in activities in this State which would subject a C Corporation to the requirement to file a return under [Section number--taxation of C Corporation] or which has a shareholder resident in this state shall file with the [State taxing authority] an annual return, in the form prescribed by the [State taxing authority], on or before the due date prescribed for the filing of C Corporation returns under [Section number--corporate tax return filing date]. The return shall set forth the name, address, social security or federal identification number, and last known address or residence of each shareholder; the Income Attributable to the State and Income Not Attributable to the State with respect to each shareholder as determined under this Part; the modifications required by Section 1002 of this Part; and such other information as the [State taxing authority] may by regulations prescribe. The S Corporation shall, on or before the day on which such return is filed, furnish to each person who was a shareholder during the year a copy of such information shown on the return as the [State taxing authority] may by regulation prescribe. The S Corporation shall also maintain the accumulated adjustments account described in Section 1006(c)(2) of this Part.

Attachment 4

626.

Proposed Statutory Language on Reporting Options for Non-resident Members of Pass-through Entities with Withholding Requirement
Adopted December 18, 2003

Section 1. Definitions.

A. "Pass-through entity" means a corporation that for the applicable tax year is treated as an S Corporation under [IRC §1362(a), or State Tax Code §], and a general partnership, limited partnership, limited liability partnership, trust, or limited liability company that for the applicable tax year is not taxed as a corporation [for federal tax purposes] [under the state's check-the-box regulation];

B. "Member" means [*optional additional language*: an individual who is] a shareholder of an S corporation; a partner in a general partnership, a limited partnership, or a limited liability partnership; a member of a limited liability company; or a beneficiary of a trust;

C. "Nonresident" means an individual who is not a resident of or domiciled in the state, a business entity that does not have its commercial domicile in the state, and a trust not organized in the state.

Section 2. Composite Return Authorized.

A. A pass-through entity may file a composite income tax return on behalf of electing nonresident members reporting and paying income tax at the highest marginal rate provided in [state tax rate provision] on the members' pro rata or distributive shares of income of the pass-through entity from doing business in, or deriving income from sources within, this State.

B. A nonresident member whose only source of income within a state is from one or more pass-through entities may elect to be included in a composite return filed pursuant to this section.

C. A nonresident member that has been included in a composite return may file an individual income tax return and shall receive credit for tax paid on the member's behalf by the pass-through entity.

Section 3. Withholding Required.

A. A pass-through entity shall withhold income tax at the highest tax rate provided in [section x for individuals or section y for corporations or section z for other entities] on the share of income of the entity distributed to each nonresident member and pay the withheld amount in the manner prescribed by the [tax agency]. The pass-through entity shall be liable to the [state] for the payment of the tax required to be withheld under this section and shall not be liable to such member for the amount withheld and paid over in compliance with this section. A member of a pass-through entity that is itself a pass-through entity (a "lower-tier pass-through entity") shall be subject to this same requirement to withhold and pay over income tax on the share of income distributed by the lower-tier pass-through entity to each of its nonresident members. The [tax agency] shall apply tax withheld and paid over by a pass-through entity on distributions to a lower-tier pass-through entity to the withholding required of that lower-tier pass-through entity.

B. A pass-through entity shall, at the time of payment made pursuant to this section, deliver to the department a return upon a form prescribed by the department showing the total amounts paid or credited to its nonresident members, the amount withheld in accordance with this section, and any other information the department may require. A pass-through entity shall furnish to its nonresident member annually, but not later than the fifteenth day of the third month after the end of its taxable year, a record of the amount of tax withheld on behalf of such member on a form prescribed by the department.

C. Notwithstanding subsection A, a pass-through entity is not required to withhold tax for a nonresident member if

(1) the member has a pro rata or distributive share of income of the pass-through entity from doing business in, or deriving income from sources within, this State of less than $1,000 per annual accounting period;

(2) the [tax agency] has determined by regulation, ruling or instruction that the member's income is not subject to withholding; or

(3) the member elects to have the tax due paid as part of a composite return filed by the pass-through entity under Section 2; or

(4) the entity is a publicly traded partnership as defined by Section 7704(b) of the Internal Revenue Code that is treated as a partnership for the purposes of the Internal Revenue Code and that has agreed to file an annual information return reporting the name, address, taxpayer identification number and other information requested by the [tax department] of each unitholder with an income in the state in excess of $500.

States That May Require Withholding From Pass-Through Entities

State	S Corporations	Partnerships/LLCs
Alabama	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) or fails to pay tax - Payment made with composite return, based on net income, and payable on return's due date (15^{th} day of 3^{rd} month after end of taxable year)	- Required if noncorporate nonresident owner doesn't file consent to pay tax (attached to partnership return) or fails to pay tax - Payment made with composite return, based on net income, and payable on return's due date (15^{th} day of 4^{th} month after end of taxable year)
Arkansas	- Not required - If any shareholder doesn't file a return and pay tax due, S election may be revoked and corporation subject to tax on the income	- Not required - Composite return may be permitted
California	- Generally not required - Nonresident individuals may file composite returns; estimated tax payments may be required	- Required on distributions of current and prior years' income if owner doesn't certify that tax was paid on the income - Required if nonresident corporate or noncorporate LLC member doesn't file consent to pay tax or fails to pay tax - Nonresident individuals may file composite returns; estimated tax payments may be required
Colorado	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) or doesn't participate in composite return - Payment based on net income, payable on return's due date (15^{th} day of 4^{th} month after end of taxable year) - Estimated tax payments may be required for composite returns	- Required if noncorporate nonresident owner doesn't file consent to pay tax (attached to partnership return) or doesn't participate in composite return - Payment based on net income, payable on return's due date (15^{th} day of 4^{th} month after end of taxable year) - Estimated tax payments may be required for composite returns

State	S Corporations	Partnerships/LLCs
Connecticut	- Required if nonresident owner doesn't participate in composite return - Payments based on net income, payable quarterly for nonresident owners whether or not they participate in composite return	- Required if noncorporate nonresident owner doesn't participate in composite return - Payments based on net income, payable quarterly for nonresident owners whether or not they participate in composite return
Delaware	- Required for nonresident owners - Payments based on net income, payable quarterly for nonresident owners whether or not they participate in composite return	- Not required
Georgia	- Required if nonresident owner doesn't participate in composite return - Payment based on distributions, payable within 30 days of the calendar month in which the distribution is paid - Quarterly estimated tax payments may be required for composite returns - S election terminated if owner doesn't file consent to pay tax (attached to S corporation's return)	- Required if noncorporate nonresident owner doesn't participate in composite return - Payment based on distributions, payable within 30 days of the calendar month in which the distribution is paid - Quarterly estimated tax payments may be required for composite returns
Hawaii	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) - Payment based on net income, payable on return's due date (20th day of 4th month after end of taxable year) - S corporation may file composite income tax return on behalf of nonresident individual owners; estimated payments may be required	- Not required - Partnership may file composite income tax return on behalf of nonresident individual owners; estimated payments may be required

State	S Corporations	Partnerships/LLCs
Idaho	- Not required - If nonresident individual owner doesn't file a return or elect to participate in composite return, entity subject to tax on the income on its return	- Not required - If nonresident individual owner doesn't file a return or elect to participate in composite return, entity subject to tax on the income on its return
Indiana	- Required for nonresident owners - Payments payable quarterly (last day of month following calendar quarter) or annually (15th day of 3rd month after end of taxable year), depending on how often distributions are paid or credited - Nonresident individuals may participate in composite return	- Required for nonresident owners - Payments payable quarterly (last day of month following calendar quarter) or annually (15th day of 3rd month after end of taxable year, depending on how often distributions are paid or credited - Nonresident individuals may participate in composite return
Iowa	- Not required - Nonresident individual owners may be permitted or required to file composite returns	- Not required - Nonresident individual owners may be permitted or required to file composite returns
Kansas	- Required if nonresident owner doesn't file consent to pay tax (attached to withholding return) - Payment made with withholding form, based on net income, and payable on corporation return's due date (15th day of 4th month after end of taxable year) - Nonresident individual owners may file composite return	- Required if nonresident owner doesn't file consent to pay tax (attached to withholding return) - Payment made with withholding form, based on net income, and payable on entity return's due date (15th day of 4th month after end of taxable year) - Nonresident individual owners may file composite return
Kentucky	- Required for nonresident individual owners - Payment made with withholding form, based on net income, and payable by 15th day of 4th month after end of taxable year - Nonresident individual owners may file composite return	- Required for nonresident individual owners - Payment made with withholding form, based on net income, and payable by 15th day of 4th month after end of taxable year - Nonresident individual owners may file composite return

State	S Corporations	Partnerships/LLCs
Louisiana	- Not required - If nonresident owner doesn't file a return or pay tax due, entity subject to tax on the income on its return	- Not required - Nonresident individual owners required to participate in composite return if they don't file consent (by due date of entity's return) to pay tax - Composite payment due with composite return
Maine	- Required if nonresident owner doesn't consent to participate in composite return and corporation doesn't make quarterly estimated payments - Payment made with withholding form due January 31	- Required if nonresident owner doesn't consent to participate in composite return and entity doesn't make quarterly estimated payments - Payment made with withholding form due January 31
Maryland	- Required for nonresident individual owners - Estimated payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return	- Required for nonresident individual owners - Estimated payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return
Michigan	- Required for nonresident individual owners - Payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return	- Required for nonresident individual owners - Payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return
Minnesota	- Required if nonresident owner doesn't consent to file composite return - Payment made with S corporation return, based on net income, and payable on return's due date (15th day of 3rd month after end of taxable year) - Estimated payments for composite returns based on net income, payable quarterly	- Required if nonresident individual owner doesn't consent to file composite return - Payment made with partnership's return, based on net income, and payable on return's due date (15th day of 4th month after end of taxable year) - Estimated payments for composite returns based on net income, payable quarterly

State	S Corporations	Partnerships/LLCs
Mississippi	- Required if nonresident owner doesn't consent to pay tax or participate in composite return - Payment based on net income, payable by return's due date - Estimated payments for composite returns based on net income, payable quarterly	- Required if nonresident individual owner doesn't consent to pay tax or participate in composite return - Payment based on net income, payable by return's due date - Estimated payments for composite returns based on net income, payable quarterly
Missouri	- Required if nonresident individual owner doesn't file consent to pay tax or participate in composite return - Payment based on net income, payable on return's due date or extended due date - Estimated payments for composite returns based on net income, payable quarterly	- Required if nonresident individual owner doesn't file consent to pay tax or participate in composite return - Payment based on net income, payable on return's due date or extended due date - Estimated payments for composite returns based on net income, payable quarterly
Montana	- Required if nonresident individual owner doesn't consent to pay tax (attached to S corporation return) or participate in composite return - Payment based on net income, payable on return's due date - Estimated payments based on net income, payable quarterly	- Required if nonresident individual owner doesn't consent to pay tax (attached to partnership return) or participate in composite return - Payment based on net income, payable on return's due date - Estimated payments based on net income, payable quarterly
Nebraska	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) - Payment made with return, based on net income, payable on return's due date (15th day of 3rd month after end of taxable year)	- Required if nonresident individual doesn't file consent to pay tax (attached to partnership return) - Payment made with return, based on net income, payable on return's due date (15th day of 4th month after end of taxable year)

State	S Corporations	Partnerships/LLCs
New Jersey	- Required to remit tax on behalf of certain nonresident owners - Payment based on net income - Nonresident individual owners may participate in composite return - Quarterly estimated payments may be required	- Required to remit tax on behalf of certain nonresident owners - Payment based on net income - Nonresident individual owners may participate in composite return - Quarterly estimated payments may be required
New Mexico	- Required if nonresident owner doesn't consent to pay tax - Payment based on net income, payable on return's due date - Nonresident individual owners may file composite return	- Required if nonresident owner doesn't consent to pay tax - Payment based on net income, payable on return's due date - Nonresident individual owners may file composite return
New York	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) - Payments based on net income, payable quarterly	- Required if nonresident owner doesn't file consent to pay tax (attached to partnership return) - Payments based on net income, payable quarterly
North Carolina	- If nonresident owner doesn't file consent to pay tax by due date of corporation's return, corporation liable for tax - Nonresident shareholders may file composite return; estimated payments not required	- Required if nonresident owner doesn't file consent to pay tax by due date of partnership's return - Payment based on net income, payable on return's due date
Ohio	- Required if nonresident individual owner doesn't participate in composite return - Estimated payments based on net income, payable quarterly for both withholding and composite returns	- Required if nonresident individual owner doesn't participate in composite return - Estimated payments based on net income, payable quarterly for both withholding and composite returns

State	S Corporations	Partnerships/LLCs
Oklahoma	- Required if nonresident owner doesn't file consent to pay tax - Payment based on distributions, payable by last day of month following calendar quarter in which distribution is made - Corporation liable for unpaid tax of nonresident owner	- Required if nonresident owner doesn't file consent to pay tax or participate in composite return - Payment based on distributions, payable by last day of month following calendar quarter in which distribution is made - Composite return part of partnership return; estimated payments may be required
Pennsylvania	- Required from nonresident owners - Payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return	- Required from nonresident owners - Payments based on net income, payable quarterly - Nonresident individual owners may participate in composite return
Rhode Island	- Required if nonresident owner doesn't file consent to pay tax (attached to business return) - Payment based on net income, payable on return's due date (15th day of 3rd month after end of taxable year)	- Required if nonresident individual owner of LLC doesn't file consent to pay tax (attached to business return) - Payment based on net income, payable on return's due date (15th day of 3rd month after end of taxable year) - Not required for partnerships
South Carolina	- Required if nonresident owner doesn't consent to pay tax (attach to withholding return) or participate in composite return - Payments based on net income, payable on return's due date (15th day of 3rd month after end of taxable year) - Nonresident individual owners may participate in composite return	- Required if nonresident owner doesn't consent to pay tax (attach to partnership return) or participate in composite return - Payments based on net income, payable on return's due date (15th day of 4th month after end of taxable year) - Nonresident noncorporate owners may participate in composite return
Utah	- Required from nonresident owners - Payment based on net income, payable on return's due date	- Nonresident individual owners may participate in composite return

State	S Corporations	Partnerships/LLCs
Vermont	- Required from nonresident owners - Payments based on net income, payable quarterly - Pre-approved nonresident individual owners may participate in composite return	- Required from nonresident owners - Payments based on net income, payable quarterly - Pre-approved nonresident individual owners may participate in composite return
Virginia	- Not required - Nonresident individual owners may receive permission to file composite return; estimated payments may be required	- Not required - Nonresident individual owners may receive permission to file composite return; estimated payments may be required
West Virginia	- Required if nonresident owner doesn't file consent to pay tax (attached to S corporation return) or participate in composite return - Payment based on net income, payable on return's due date (15th day of 3rd month after end of taxable year) - Nonresident individual owners may participate in composite return	- Required if nonresident owner doesn't file consent to pay tax (attached to partnership return) or participate in composite return - Payment based on net income, payable on return's due date (15th day of 4th month after end of taxable year) - Nonresident individual owners may participate in composite return

Sources: *2004 Multistate Corporate Tax Guide*, Aspen Publishers
State Tax Treatment of LLCs and LLPs - Nonresident Member/Partner Withholding, BNATAX Management
State web sites

State of Wisconsin
2005 – 2006 LEGISLATURE

LRB–0306/?
JK:...:...
wlj

DOA:......Justus, BB0068 – Require withholding from nonresident members of pass–through entities

FOR 2005–07 BUDGET -- NOT READY FOR INTRODUCTION

in 9-28-04

D-N

DO NOT GEN

AN ACT ...; **relating to:** the budget.

Analysis by the Legislative Reference Bureau

TAXATION

INCOME TAXATION

This bill requires partnerships, limited liability companies, tax–option corporations, estates, and trusts that are treated as a pass–through entities for federal income tax purposes to withhold income taxes from income that the entity distributes to a nonresident partner, member, shareholder, or beneficiary.

For further information see the ***state*** fiscal estimate, which will be printed as an appendix to this bill.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

SECTION 1. 71.775 of the statutes is created to read:

71.775 Withholding from nonresident members of pass–through entities. (1) DEFINITION. In this section:

(a) "Nonresident" includes an individual who is not domiciled in this state; a partnership, limited liability company, or corporation whose commercial domicile is outside the state; and an estate or trust that is a nonresident under s. 71.74 (1) to (3m).

(b) "Pass–through entity" means a partnership, limited liability company, tax–option corporation, estate, or trust that is treated as a pass–through entity for federal income tax purposes.

(2) WITHHOLDING TAX IMPOSED. (a) For the privilege of doing business in this state or deriving income from property located in this state, a pass–through entity that has Wisconsin income for the taxable year that is allocable to a nonresident partner, member, shareholder, or beneficiary shall pay a withholding tax. The amount of the tax imposed under this subsection to be withheld from the income distributed to each nonresident partner, member, shareholder, or beneficiary is equal to the nonresident partner's, member's, shareholder's, or beneficiary's share of income attributable to this state, multiplied by the following:

that is a pass-through entity

1. For an individual, estate, or trust, the highest tax rate for a single individual for the taxable year under s. 71.06.

2. For a partnership, limited liability company, or tax–option corporation, the highest tax rate for the taxable year under s. 71.27.

(b) A pass–through entity that is also a member of another pass–through entity is subject to withholding under this subsection and shall pay the tax based on the share of income that is distributable to each of the entity's nonresident partners, members, shareholders, or beneficiaries.

(3) EXEMPTIONS. (a) A nonresident partner's, member's, shareholder's, or beneficiary's share of income from the pass–through entity that is attributable to this

state shall not be included in determining the withholding under sub. (2) if any of the following applies:

1. The partner, member, shareholder, or beneficiary is exempt from taxation under this chapter. For purposes of this subdivision, the pass–through entity may rely on a written statement from the partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter, if the pass–through entity attaches a copy of the statement to its return for the taxable year and if the statement specifies the name, address, federal employer identification number, and reason for claiming an exemption for each partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter.

2. The partner, member, shareholder, or beneficiary has no Wisconsin income other than his or her share of income from the pass–through entity that is attributable to this state and his or her share of such income is less than $1,000.

(b) A pass–through entity that is a joint venture is not subject to the withholding under sub. (2), if the pass–through entity has elected not to be treated as a partnership under section 761 of the Internal Revenue Code.

(4) ADMINISTRATION. (a) Each pass–through entity that is subject to the withholding under sub. (2) shall pay the amount of the tax withheld to the department no later than:

1. For tax–option corporations, the 15th day of the 3rd month following the close of the taxable year.

2. For partnerships, limited liability companies, estates and trusts, the 15th day of the 4th month following the close of the taxable year.

(b) 1. If the pass–through entity has an extension of time to file its return, the tax withheld under sub. (2) is due on the unextended due date of the entity's return as provided under s. 71.13 (1), 71.20 (1), or 71.24 (1).

2. A pass–through entity that pays the tax withheld under sub. (2) as provided under subd. 1. is not subject to an underpayment of estimated tax under s. 71.09 or 71.29, if 90 percent of the tax that is due for the current taxable year is paid by the unextended due date or if 100 percent of the tax that is due for the taxable year immediately preceding the current taxable year is paid by the unextended due date and the taxable year immediately preceding the current taxable year was a 12 month period. Interest at the rate 12 percent shall be imposed on the unpaid amount of the tax withheld under sub. (2) during any extension period and interest at the rate of 18 percent shall be imposed on the unpaid amount of the tax withheld under sub. (2) for the period beginning with the extended due date and ending with the date that the unpaid amount is paid in full.

(c) On or before the unextended due date of the entity's return, a pass–through entity that withholds tax under sub. (2) shall annually notify each of its nonresident partners, members, shareholders, or beneficiaries of the amount of the tax withheld under sub. (2) that the pass–through entity paid on the nonresident partner's, member's, shareholder's, or beneficiary's behalf. The pass–through entity shall provide a copy of the notice to the department with the return that it files for the taxable year.

(d) A nonresident partner, member, shareholder, or beneficiary of a pass–through entity may claim a credit, as prescribed by the department, on his or her Wisconsin income or franchise tax return for the amount withheld under sub. (2) on his or her behalf. For purposes of this paragraph, the amount withheld under sub.

(2) is considered to be paid on the last day of the pass–through entity's taxable year for which the tax is paid.

(e) Any tax withheld under this section shall be held in trust for this state and a pass–through entity subject to withholding under this section shall be liable to the department for the payment of the tax withheld. No partner, member, shareholder, or beneficiary of a pass–through entity shall have any right of action against the pass–through entity with respect to any amount withheld and paid in compliance with this section.

(f) If a pass–through entity subject to withholding under this section fails to withhold tax as required by this section, the pass–through entity shall be liable for any tax, interest, and ~~penlites~~ penalties. If a nonresident partner, member, shareholder, or beneficiary of the pass–through entity files a return and pays the tax due, the pass–through entity shall not be liable for the tax, but shall be liable for any interest and penalties otherwise applicable for failure to withhold, as provided under ss. 71.82 (2) (d) and 71.83.

SECTION 9341. Initial applicability; revenue.

(1) WITHHOLDING TAXES FROM NONRESIDENT MEMBERS OF PASS–THROUGH ENTITIES. The treatment of section 71.775 of the statutes first applies to taxable years beginning on January 1, 2005.

(END)

Drafter's Note
from the
Legislative Reference Bureau

LRB-0306/?dn
JK:/...:...
wlj

Sarah:

Please review this draft carefully to ensure that it is consistent with your intent.

Joseph T. Kreye
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Drafter's Note
from the
Legislative Reference Bureau

LRB–0306/1dn
JK:wlj:pg

October 19, 2004

Sarah:

Please review this draft carefully to ensure that it is consistent with your intent.

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Kreye, Joseph

From: Justus, Sarah
Sent: Thursday, November 04, 2004 11:36 AM
To: Kreye, Joseph
Subject: FW: LRB Draft: 05-0306/1 Require withholding from nonresident members of pass-through entities

05-0306/1 05-0306/1dn

Comments from DOR on the draft.

Thanks!

-----Original Message-----
From: Lashore, Patricia M
Sent: Wednesday, November 03, 2004 4:23 PM
To: Justus, Sarah
Cc: Collier, Dennis J; Gates-Hendrix, Sherrie
Subject: LRB Draft: 05-0306/1 Require withholding from nonresident members of pass-through entities

Here are comments on the draft from Carol Held, IS&E Administration:

1. Page 2, line 13: The word "distributed" should be changed to "distributable". We don't want a pass-through entity to avoid the withholding tax by not making any distributions of income before the end of its taxable year.

2. Page 4, line 15: The phrase "unextended due date" should be changed to the "due date including extensions". Since the entities don't have to furnish a K-1 reporting the partner's, member's, shareholder's, or beneficiary's share of the income to that person until the entity files its tax return, we don't want these entities to have to provide a separate withholding document prior to the date that they furnish the K-1.

State of Wisconsin
2005 – 2006 LEGISLATURE

LRB–0306/1
JK:wlj:pg

RMR

DOA:......Justus, BB0068 – Require withholding from nonresident members of pass–through entities

FOR 2005–07 BUDGET –– NOT READY FOR INTRODUCTION

11-04-04

SOON

DO NOT GEN

AN ACT ...; **relating to:** the budget.

Analysis by the Legislative Reference Bureau

TAXATION

INCOME TAXATION

This bill requires a partnership, a limited liability company, a tax–option corporation, an estate, or a trust that is treated as a pass–through entity for federal income tax purposes to withhold income taxes from income that the entity distributes to a nonresident partner, member, shareholder, or beneficiary.

For further information see the ***state*** fiscal estimate, which will be printed as an appendix to this bill.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

SECTION 1. 71.775 of the statutes is created to read:

71.775 Withholding from nonresident members of pass–through entities. (1) DEFINITIONS. In this section:

(a) "Nonresident" includes an individual who is not domiciled in this state; a partnership, limited liability company, or corporation whose commercial domicile is outside the state; and an estate or a trust that is a nonresident under s. 71.14 (1) to (3m).

(b) "Pass–through entity" means a partnership, a limited liability company, a tax–option corporation, an estate, or a trust that is treated as a pass–through entity for federal income tax purposes.

(2) WITHHOLDING TAX IMPOSED. (a) For the privilege of doing business in this state or deriving income from property located in this state, a pass–through entity that has Wisconsin income for the taxable year that is allocable to a nonresident partner, member, shareholder, or beneficiary shall pay a withholding tax. The amount of the tax imposed under this subsection to be withheld from the income ~~distributed~~ distributable to each nonresident partner, member, shareholder, or beneficiary is equal to the nonresident partner's, member's, shareholder's, or beneficiary's share of income attributable to this state, multiplied by the following:

1. For an individual, an estate, or a trust that is a pass–through entity, the highest tax rate for a single individual for the taxable year under s. 71.06.

2. For a partnership, a limited liability company, or a tax–option corporation that is a pass–through entity, the highest tax rate for the taxable year under s. 71.27.

(b) A pass–through entity that is also a member of another pass–through entity is subject to withholding under this subsection and shall pay the tax based on the share of income that is distributable to each of the entity's nonresident partners, members, shareholders, or beneficiaries.

(3) EXEMPTIONS. (a) A nonresident partner's, member's, shareholder's, or beneficiary's share of income from the pass–through entity that is attributable to this

state shall not be included in determining the withholding under sub. (2) if any of the following applies:

1. The partner, member, shareholder, or beneficiary is exempt from taxation under this chapter. For purposes of this subdivision, the pass–through entity may rely on a written statement from the partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter, if the pass–through entity attaches a copy of the statement to its return for the taxable year and if the statement specifies the name, address, federal employer identification number, and reason for claiming an exemption for each partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter.

2. The partner, member, shareholder, or beneficiary has no Wisconsin income other than his or her share of income from the pass–through entity that is attributable to this state and his or her share of such income is less than $1,000.

(b) A pass–through entity that is a joint venture is not subject to the withholding under sub. (2), if the pass–through entity has elected not to be treated as a partnership under section 761 of the Internal Revenue Code.

(4) ADMINISTRATION. (a) Each pass–through entity that is subject to the withholding under sub. (2) shall pay the amount of the tax withheld to the department no later than:

1. For tax–option corporations, the 15th day of the 3rd month following the close of the taxable year.

2. For partnerships, limited liability companies, estates, and trusts, the 15th day of the 4th month following the close of the taxable year.

(b) 1. If the pass–through entity has an extension of time to file its return, the tax withheld under sub. (2) is due on the unextended due date of the entity's return as provided under s. 71.13 (1), 71.20 (1), or 71.24 (1).

2. A pass–through entity that pays the tax withheld under sub. (2) as provided under subd. 1. is not subject to an underpayment of estimated tax under s. 71.09 or 71.29, if 90 percent of the tax that is due for the current taxable year is paid by the unextended due date or if 100 percent of the tax that is due for the taxable year immediately preceding the current taxable year is paid by the unextended due date and the taxable year immediately preceding the current taxable year was a 12–month period. Interest at the rate 12 percent shall be imposed on the unpaid amount of the tax withheld under sub. (2) during any extension period and interest at the rate of 18 percent shall be imposed on the unpaid amount of the tax withheld under sub. (2) for the period beginning with the extended due date and ending with the date that the unpaid amount is paid in full. ; including extensions;

(c) On or before the ~~unextended~~ due date of the entity's return, a pass–through entity that withholds tax under sub. (2) shall annually notify each of its nonresident partners, members, shareholders, or beneficiaries of the amount of the tax withheld under sub. (2) that the pass–through entity paid on the nonresident partner's, member's, shareholder's, or beneficiary's behalf. The pass–through entity shall provide a copy of the notice to the department with the return that it files for the taxable year.

(d) A nonresident partner, member, shareholder, or beneficiary of a pass–through entity may claim a credit, as prescribed by the department, on his or her Wisconsin income or franchise tax return for the amount withheld under sub. (2) on his or her behalf. For purposes of this paragraph, the amount withheld under sub.

(2) is considered to be paid on the last day of the pass–through entity's taxable year for which the tax is paid.

(e) Any tax withheld under this section shall be held in trust for this state, and a pass–through entity subject to withholding under this section shall be liable to the department for the payment of the tax withheld. No partner, member, shareholder, or beneficiary of a pass–through entity shall have any right of action against the pass–through entity with respect to any amount withheld and paid in compliance with this section.

(f) If a pass–through entity subject to withholding under this section fails to withhold tax as required by this section, the pass–through entity shall be liable for any tax, interest, and penalties. If a nonresident partner, member, shareholder, or beneficiary of the pass–through entity files a return and pays the tax due, the pass–through entity shall not be liable for the tax, but shall be liable for any interest and penalties otherwise applicable for failure to withhold, as provided under ss. 71.82 (2) (d) and 71.83.

SECTION 9341. Initial applicability; revenue.

(1) WITHHOLDING TAXES FROM NONRESIDENT MEMBERS OF PASS–THROUGH ENTITIES. The treatment of section 71.775 of the statutes first applies to taxable years beginning on January 1, 2005.

(END)

State of Wisconsin
2005 – 2006 LEGISLATURE

LRB–0306/2
JK:wlj:rs

DOA:......Justus, BB0068 – Require withholding from nonresident members of pass–through entities

FOR 2005–07 BUDGET -- NOT READY FOR INTRODUCTION

AN ACT ...; **relating to:** the budget.

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(2) WITHHOLDING TAX IMPOSED. (a) For the privilege of doing business in this state or deriving income from property located in this state, a pass–through entity that has Wisconsin income for the taxable year that is allocable to a nonresident partner, member, shareholder, or beneficiary shall pay a withholding tax. The amount of the tax imposed under this subsection to be withheld from the income distributable to each nonresident partner, member, shareholder, or beneficiary is equal to the nonresident partner's, member's, shareholder's, or beneficiary's share of income attributable to this state, multiplied by the following:

1. For an individual, an estate, or a trust that is a pass–through entity, the highest tax rate for a single individual for the taxable year under s. 71.06.

2. For a partnership, a limited liability company, or a tax–option corporation that is a pass–through entity, the highest tax rate for the taxable year under s. 71.27.

(b) A pass–through entity that is also a member of another pass–through entity is subject to withholding under this subsection and shall pay the tax based on the share of income that is distributable to each of the entity's nonresident partners, members, shareholders, or beneficiaries.

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state shall not be included in determining the withholding under sub. (2) if any of the following applies:

1. The partner, member, shareholder, or beneficiary is exempt from taxation under this chapter. For purposes of this subdivision, the pass–through entity may rely on a written statement from the partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter, if the pass–through entity attaches a copy of the statement to its return for the taxable year and if the statement specifies the name, address, federal employer identification number, and reason for claiming an exemption for each partner, member, shareholder, or beneficiary claiming to be exempt from taxation under this chapter.

2. The partner, member, shareholder, or beneficiary has no Wisconsin income other than his or her share of income from the pass–through entity that is attributable to this state and his or her share of such income is less than $1,000.

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(c) On or before the due date, including extensions, of the entity's return, a pass–through entity that withholds tax under sub. (2) shall annually notify each of its nonresident partners, members, shareholders, or beneficiaries of the amount of the tax withheld under sub. (2) that the pass–through entity paid on the nonresident partner's, member's, shareholder's, or beneficiary's behalf. The pass–through entity shall provide a copy of the notice to the department with the return that it files for the taxable year.

(d) A nonresident partner, member, shareholder, or beneficiary of a pass–through entity may claim a credit, as prescribed by the department, on his or her Wisconsin income or franchise tax return for the amount withheld under sub. (2) on his or her behalf. For purposes of this paragraph, the amount withheld under sub.

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