



Matt & Matt in the Morning



Personal Income Tax Residency & Pass-Through Entity Nuts and Bolts

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Department of
Taxation

Overview

- Income Tax Residency
 - R.C. 5747.24
 - Presumption of Domicile
 - Contact Periods
 - Ohio Adm.Code 5703-7-16
 - Items that cannot determine domicile
 - Items that can determine domicile
- Pass-Through Entity Overview
 - Purpose of the Taxes
 - Comparison of the Taxes
 - Interplay with Ohio's SBD and BID



5747.24 Presumption of Domicile

Contact Periods 5747.24(A)

- (1) An individual “has one contact period in this state” if the individual is away overnight from the individual’s abode located outside this state and while away overnight from that abode spends at least some portion, however minimal, of each of two consecutive days in the state.
- (2) An individual is considered to be “away overnight from the individual’s abode located outside this state” if the individual is away from the individual’s abode located outside this state for a continuous period of time, however minimal, beginning at any time on one day and ending at any time on the next day.

Less Than 213 Contact Periods 5747.24

- (C) An individual who during a taxable year has fewer than two hundred thirteen contact periods in this state, which need not be consecutive, and who is not irrebuttably presumed under division (B) of this section to be not domiciled in this state with respect to that taxable year, is presumed to be domiciled in this state for the entire taxable year, except as provided in division (B)(2) of this section. An individual can rebut this presumption for any portion of the taxable year only with a **preponderance of the evidence to the contrary**. An individual who rebuts the presumption under this division for any portion of the taxable year is presumed to be domiciled in this state for the remainder of the taxable year for which the individual does not provide a preponderance of the evidence to the contrary.

More Than 213 Contact Periods

5747.24

- (D) An individual who during a taxable year has at least two hundred thirteen contact periods in this state, which need not be consecutive, is presumed to be domiciled in this state for the entire taxable year, except as provided in division (B)(2) of this section. An individual can rebut this presumption for any portion of the taxable year only with **clear and convincing evidence to the contrary**. An individual who rebuts the presumption under this division for any portion of the taxable year is presumed to be domiciled in this state for the remainder of the taxable year for which the individual does not provide clear and convincing evidence to the contrary.

Affidavit

5747.24(B)

- (1) Except as provided in division (B)(2) of this section, an individual who during a taxable year has no more than two hundred twelve contact periods in this state, which need not be consecutive, and who during the entire taxable year has at least one abode outside this state, is presumed to be not domiciled in this state during the taxable year if, on or before the fifteenth day of the fourth month following the close of the taxable year, the individual files with the tax commissioner, on the form prescribed by the commissioner, a statement from the individual verifying that the individual was not domiciled in this state under this division during the taxable year. In the statement, the individual shall verify both of the following:
 - (a) During the entire taxable year, the individual was not domiciled in this state;
 - (b) During the entire taxable year, the individual had at least one abode outside this state. The individual shall specify in the statement the location of each such abode outside this state.
- The presumption that the individual was not domiciled in this state is irrebuttable unless the individual fails to timely file the statement as required or makes a false statement. If the individual fails to file the statement as required or makes a false statement, the individual is presumed under division (C) of this section to have been domiciled in this state the entire taxable year.

5703-7-16 Personal Income Tax: Determination of Resident Status

- (A) The following factors shall not be considered in making a determination of an individual's domicile under division (c) or (d) of section 5747.24 of the Revised Code:



5703-7-16 Personal Income Tax: Determination of Resident Status



- (1) The location of financial institutions in which the individual or the individual's spouse have any accounts, including, but not limited to, checking, savings, certificates of deposit, or individual retirement accounts.

5703-7-16 Personal Income Tax: Determination of Resident Status

- (2) The location of issuers of credit cards to the individual or the individual's spouse or any other persons making installment loans to the individual or the individual's spouse.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (3) The location of institutional lenders which have made loans to or loans which are guaranteed by the individual or the individual's spouse.



5703-7-16 Personal Income Tax: Determination of Resident Status



- (4) The location of investment facilities, brokerage firms, realtors, financial advisors or consultants used by the individual or the individual's spouse.

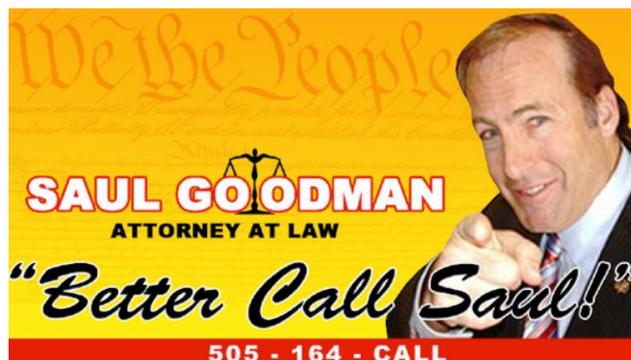
5703-7-16 Personal Income Tax: Determination of Resident Status

- (5) The location of either the insurance company that issued or the insurance agent that sold any policy of insurance to the individual or the individual's spouse including, but not limited to, life, health, disability, automobile, or homeowner's insurance.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (6) The location of law firms, accounting firms, and similar professionals utilized by the individual or the individual's spouse for legal, tax, accounting, financial, or retirement services.



5703-7-16 Personal Income Tax: Determination of Resident Status



- (7) The location of physicians, dentists, osteopaths, optometrists, or other health care providers, or veterinarians utilized by the individual or the individual's spouse.

5703-7-16 Personal Income Tax: Determination of Resident Status

- (8) The location of organizations described in section 501(c) of the Internal Revenue Code, *** to which the individual or the individual's spouse make contributions or other payments or in which they participate as a congregant, member, board member, committee member, adviser, or consultant provided that participation does not exceed attendance at more than twelve meetings or functions of any one such organization during a calendar year.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (9) The location of funeral facilities or the burial plot of the individual or the individual's spouse.



5703-7-16 Personal Income Tax: Determination of Resident Status



- (10) The location of business ventures or business entities in which the individual or the individual's spouse hold board membership unless the individual or the individual's spouse exercise significant control, either individually or jointly, over the affairs of the entity.

5703-7-16 Personal Income Tax: Determination of Resident Status

- (11) The location, place of business, or place of organization or incorporation of a corporation, partnership, limited liability company, or other business entity or business venture in which the individual or the individual's spouse is a shareholder or limited partner unless the individual or the individual's spouse exercises significant control



5703-7-16 Personal Income Tax: Determination of Resident Status

- (12) The recitation of residency or domicile in a will, trust, or other estate planning document.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (13) The location of the individual's friends, dependents as defined in section 152 of the Internal Revenue Code, and family members other than his or her spouse, if not legally separated from his or her spouse



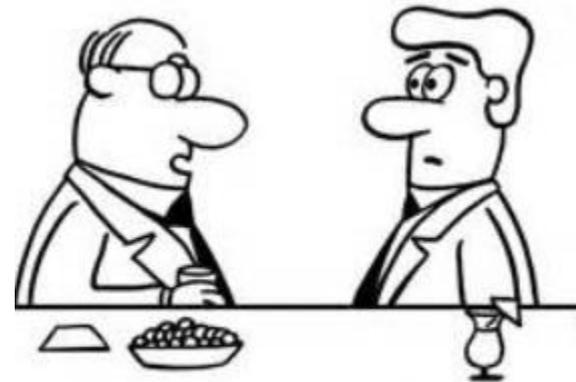
5703-7-16 Personal Income Tax: Determination of Resident Status

- (14) The location of educational institutions attended by the individual's dependents as defined in section 152 of the Internal Revenue Code, unless those dependents pay tuition at that educational institution based on the residency of the individual or the individual's spouse in the state where the educational institution is located.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (15) The location of trustees, executors, guardians, or other fiduciaries named in estate planning documents of the individual or the individual's spouse.



This "fiduciary" thingy really complicates exploiting my job to get stinking rich.

5703-7-16 Personal Income Tax: Determination of Resident Status



- (16) The location of a business at which the individual or the individual's spouse makes purchases of tangible personal property.

5703-7-16 Personal Income Tax: Determination of Resident Status

- (17) The location where the individual married.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (18) The location or identity of recipients of political contributions made by the individual or the individual's spouse.



5703-7-16 Personal Income Tax: Determination of Resident Status

- (B) The following factors may be considered in making a determination of an individual's domicile under division (C) or (D) of section [5747.24](#) of the Revised Code:
 - The number of contact periods (determined under paragraph (C) of this rule) which the individual has in Ohio.
 - The individual's activities in tax years other than the tax year or years at issue.
 - Any other fact the tax commissioner deems relevant, excepting those set forth in paragraph (A) of this rule.



***5747.41 & 5747.08(D) Pass-Through
Entity Withholding and Composite Taxes***



Pass-Through Entity Section Overview

- Goals
 - Provide general information about pass-through entities
 - Explain the purpose of Ohio's pass-through entity taxes by comparing and contrasting them
 - Explain the interplay of these taxes with Ohio's individual income tax
- *Note* Information contained in this section is nothing new; it is simply an entry-level overview

What is a pass-through entity or “PTE”?

- Generally defined under R.C. 5733.04(O) to include:
 - S Corporations
 - Partnerships
 - Limited liability companies (LLCs)
 - Any other person, other than an individual, trust, or estate that is not a C Corporation
- PTEs are not themselves subject to income tax
 - Instead, the income “passes through” to the investors who report the income and pay the tax individually



Policy

- Again, Ohio does not levy a tax on PTEs, but instead taxes the individual investors on their share of the income.
- Issues:
 - How does Ohio know who the investors are?
 - How many investors are there and where do they reside?
 - What if the investor is a nonresident?
- Observation: PTEs operating in Ohio are easier to find than large numbers of individuals who are located across the USA



Policy

- Solution: Ohio levies two alternative taxes on PTEs with **nonresident investors**
 - The withholding tax on form 1140
 - The composite tax on form 4708
- Entity files and pays on one or both of the taxes for a given tax year
 - Both filings include investor information so that Ohio can know to whom the income will flow
- *Note* PTEs with only resident investors are not subject to PTE taxes or filing

The Withholding Tax (R.C. 5747.41; Form 1140)

- Entity pays tax on its “adjusted qualifying amount” for all “qualifying investors”
- The adjusted qualifying amount for a PTE is the aggregate distributive shares of the PTE’s investors for the entity’s tax year, subject to various adjustments and apportionment
 - R.C. 5733.40(A)
 - Different definition for certain trusts
- Qualifying investors are generally:
 - Nonresident individuals
 - Trusts
 - Other Pass-Through Entities

The Composite Tax (R.C. 5747.08(D); Form 4708)

- Paid either in supplement to, or lieu of, the PTE withholding tax
- Any PTE may **elect** to file on behalf of one or more of the entity's investors
 - Once the election is made, it is irrevocable for the tax year
 - Those “qualifying investors” not included on the 4708 must be included on an 1140
- Tax due is calculated based on the aggregate distributive shares of the PTE's investors for the entity's tax year, subject to various adjustments and apportionment
 - R.C. 5747.08(D)

PTE Income & Ohio Personal Income Tax

- Most income earned by a PTE is business income
 - PTEs are businesses and thus generate business income
 - Business income is defined at R.C. 5747.01(B)
 - Income earned by a business retains its character as it flows through to the business's investors
 - R.C. 5747.231 and *Agley v. Tracy*, 87 Ohio St.3d 265, 268 (1999).
- Personal Income Tax
 - Provides deductions for, and taxes at a preferential rate, items of business income



The 1140 vs. the 4708: A Comparison

- Now that business income, for individual income taxpayers in tax years 2016 and forward, is:
 - Deductible up to \$250,000 and
 - Taxed at a preferential rate (3% flat)

it is more important than ever that practitioners and taxpayers understand these two forms.
- *Please note*: prior years **will be different.**
 - Refer to the laws and instructions for each tax year before filing an amended return
- The next several slides will present key aspects of the two forms side by side

The 1140 vs. the 4708: A Comparison

Item 1: The Purpose

Withholding (IT 1140)

- To withhold tax due from nonresident investors
- Constitutes a “trust tax”
 - Special penalties
 - Derivative liability (responsible party)
- Must amend to report federal changes to income (RAR)

Composite (IT 4708)

- To pay the taxes due on behalf of its investors
- Not a “trust tax”
 - Normal penalties and “entity” liability applies
- Must amend to report federal changes to income (RAR)

The 1140 vs. the 4708: A Comparison

Item 2: The Filing Date

Withholding (IT 1140)

- Due the 15th day of the fourth month after the close of the entity's fiscal year
 - Fiscal year ends 3/31/15, return is due 7/15/15



Composite (IT 4708)

- Due the April 15th of the calendar year after the close of the entity's fiscal year
 - Fiscal year ends 3/31/15, return is due 4/15/16

The 1140 vs. the 4708: A Comparison

Item 3: Resident Investors

Withholding (IT 1140)

- **Cannot** include resident, individual investors' income in calculating the "adjusted qualifying amount"

Composite (IT 4708)

- **Can** include resident individual investors' income in computing the tax base
- **Not required** to do so
 - An election of convenience



The 1140 vs. the 4708: A Comparison

Item 4: The Tax Base

Withholding (IT 1140)

- “Adjusted qualifying amount”
 - Aggregation of the distributive shares of the PTE’s investors for the entity’s tax year, subject to various adjustments

Composite (IT 4708)

- Aggregate distributive share of each of those PTE investor's income taxable in this state
 - Subject to various “income tax” and “entity” adjustments

The 1140 vs. the 4708: A Comparison

Item 5: Apportionment

Withholding (IT 1140)

- Standard Apportionment
 - Weighted, **3-factor apportionment** using property, payroll, and sales
- Alternative Apportionment
 - Three types

Composite (IT 4708)

- Standard and Alternative Apportionment **same as the 1140**, except:
 - Alternative Apportionment additional fourth type:
 - “Any other method to effectuate an equitable allocation and apportionment of such business in this state.”

The 1140 vs. the 4708: A Comparison

%

Item 6: The Rate

%

Withholding (IT 1140)

- Based on the investor:
 - Withhold at 5% for individuals
 - Withhold at 8.5% for entities
- R.C. 5733.41 & 5747.41

Composite (IT 4708)

- One uniform rate for all investor types:
 - Tied to individual income tax rates
 - Currently 4.997%
- R.C. 5747.08(D); 5747.02

The 1140 vs. the 4708: A Comparison

Item 7: Credits

Withholding (IT 1140)

- PTE **cannot** reduce withholding amount due with **any** credits held by the PTE

Composite (IT 4708)

- PTE **may** offset liability with “distributive share of the business credits”
- Defined in R.C. 5747.08(D)

The 1140 vs. the 4708: A Comparison

Item 8: Claiming Payments

Withholding (IT 1140)

- **Cannot** claim credit for payments made by another PTE
 - Only previously reported income rolls up to this form



Composite (IT 4708)

- **Can claim** credit for payments made by another PTE that the filing entity invests in
 - Both previously reported income and payments roll up to this form

The 1140 vs. the 4708: A Comparison

Item 9: Estimated Payments

Withholding (IT 1140)

- Estimated payments required if certain liability thresholds are met
- R.C. 5747.43

Composite (IT 4708)

- Estimated payments required if certain liability thresholds are met
- R.C. 5747.09 (same as PIT)

The 1140 vs. the 4708: A Comparison

Item 10: Investor Filings/ Ohio Business Income Deduction

Withholding (IT 1140)

- Nonresidents individuals and other PTEs in the ownership chain **must** still file the IT 1040 and the IT 1140/ 4708, respectively
 - Individual investors can take Ohio’s SBD or BID on their IT 1040
- If there is an entity-level RAR, individual investors will need to file amended IT 1040s as well

Composite (IT 4708)

- The 4708 is a “**terminal return**”
 - I.e. no other filings are required!
 - Individual investors **may** file an IT 1040 to take Ohio’s SBD or BID
- If there is an entity-level RAR, individual investors only need to file amended IT 1040s if they originally filed them



1140 vs. the 4708: A Summary



	<u>Topic</u>	<u>The 1140</u>	<u>The 4708</u>
1	Purpose	Withholding	Composite
2	Filing Date	15 th day of Fourth Month	April 15 th after year in which fiscal year ends
3	Resident Investors	No	Yes
4	Tax Base	Adjusted qualifying amount	Aggregate distributive shares
5	Apportionment	Weighted 3 factor	Weighted 3 factor
6	Tax Rate	5% (individuals) or 8.5% (entities)	4.997% (all)
7	Credits	No	Yes
8	Claim Payments?	No	Yes
9	Est. Payments	Yes	Yes
10	Investor Filings	Must File 1040	Can File 1040