Pass-Through Entity and Trust Withholding Tax

Taxpayer

The pass-through entity tax is a system of withholding from pass-through entities designed to collect the individual income tax or corporation franchise tax that is otherwise due and payable by the entities' investors. The withholding tax is remitted by qualifying pass-through entities and qualifying trusts. A pass-through entity is an "S" corporation, partnership, or a limited liability company treated as a partnership or as an S corporation for federal income tax purposes. Many pass-through entities are not subject to the tax; see **Major Exemptions** for details.

Tax Base

The tax applies to the net sum of qualifying investors' distributive shares of the pass-through entity's income, gain, expense, and loss apportioned to Ohio. This net sum is known as the "adjusted qualifying amount."

Rates

A 5 percent withholding rate applies to the "adjusted qualifying amounts" of the entity's qualifying investors who are individuals not domiciled in Ohio.

Before 2005, an 8.5 percent entity tax rate uniformly applied to the adjusted qualifying amounts of qualifying investors that are not individuals. However, the entity tax that a qualifying pass-through entity must withhold was phased out for qualifying investors that were subject to the phase-out of the corporation franchise tax. The phase-out took place according to the following schedule:

Taxable year ending in:	Entity tax rate:
2005	6.8% (80 × 8.5%)
2006	5.1% (60 × 8.5%)
2007	3.4% (40 × 8.5%)
2008	1.7% (20 × 8.5%)
2009 and thereafter	0% (0 × 8.5%)

An 8.5 percent entity withholding rate continues to apply to the adjusted qualifying amounts of qualifying corporate investors – meaning, the relatively small number of corporations described in R.C. 5733.01(G)(1)(b) that were not subject to the corporation franchise tax phase-out, including:

- certain financial holding companies, bank holding companies and savings and loan holding companies;
- certain affiliates of these holding companies and certain affiliates of financial institutions;
- certain affiliates of insurance companies; and
- securitization companies.

No tax is due if the total adjusted qualifying amount for the taxable year is $1,000 or less.

Major Exemptions

Pass-through entities not subject to tax include:

- Pension plans and charities.
- Real estate investment trusts, regulated investment companies, and real estate mortgage investment conduits.
- Entities with no qualifying investors.

The following individuals and entities are not qualifying investors:

- Individuals who are residents of Ohio for the entire year.
- All subchapter C corporations, except for the relatively small number described in R.C. 5733.01(G)(1)(b).
- Corporations exempt from the corporation franchise tax per R.C. 5733.09, including insurance companies, dealers in intangibles, and public utilities subject to the Ohio public utility excise tax.
- Financial institutions.
- Nonresident individuals, resident and nonresident estates, and resident and nonresident trusts on whose behalf the qualifying pass-through entity files Ohio form IT-4708, "Annual Composite Income Tax Return for Investors in Pass-Through Entities."
- Investors that are "investment pass-through entities."

Neither of the above lists is exhaustive. Also, the entity tax does not apply to any pass-through entity to the extent the pass-through entity's distributive shares of income and gain pass through from that entity to another pass-through entity (the "investing entity") if the investing entity files form IT 1140 and/or form IT 4708.

Revenue

(In Millions)

The first table in this section represents Form IT 1140 tax liabilities reported for each tax year, according to the fiscal year payment associated with the tax year. For example, the liability for tax year 2008 was predominantly paid during FY 2009, so the tax year 2008 tax liability data is reported as FY 2009 revenue in the table.

Fiscal Year	Total Tax
2008	$131.0
2009	100.5
2010	90.5
2011	126.2
2012	139.6

Pass-through entities may also use Form IT 4708 to file a composite income tax return on behalf of nonresident investors. Individual income tax revenue derived from these returns is as follows:

Fiscal Year	Total Tax
2008	$134.9
2009	111.7
2010	114.5
2011	156.9
2012	155.6

Disposition of Revenue

See the **Corporation Franchise Tax** and **Individual Income Tax** chapters for details.

Payment Dates

Qualifying pass-through entities whose total adjusted qualifying amounts exceed $10,000 must make estimated quarterly tax payments. The payments are due on the 15th day of the month following the last day of each quarter of the entity's taxable year. For pass-through entities with a Jan. 1 – Dec. 31 taxable year, payments are due on April 15, July 15, Oct. 15 of the taxable year, and Jan. 15 of the following calendar year.

The annual pass-through entity tax return must be filed by the 15th day of the fourth month following the end of the entity's taxable year. For taxpayers with a Jan. 1 – Dec. 31 taxable year, the return is generally due on April 15 of the following calendar year. If the entity has an extension of time to file the federal tax return, the qualifying investor has the same extension to file the individual income tax return. However, there is no extension of time to pay.

Special Provisions/Credits

Each qualifying investor who is an individual, estate or trust may claim a refundable tax credit in a pass-through entity against their Ohio individual income tax. The credit equals the qualifying investor's proportionate share of the withholding tax and entity tax, if any.

A nonrefundable tax credit may be claimed by all other qualifying investors against their Ohio corporation franchise tax. The credit equals the investing corporation's proportionate share of the entity tax.

If, for federal income tax purposes, the investor deducts the investor's proportionate share of the withholding tax or the entity tax, the investor must add back such tax on the Ohio individual income tax return or corporation franchise tax report.

Sections of Ohio Revised Code

Sections 5733.40-.41 and 5747.40-.45.

Responsibility for Administration

Tax Commissioner.

History of Major Changes

1998	General Assembly enacts tax at a rate of 5 percent on individual qualifying investors and 8.5 percent on non-individual qualifying investors.
2002	Ohio decouples from federal accelerated depreciation laws, requiring a 5⁄6 add back for bonus depreciation.

2003	House Bill 127 revises Ohio's method of situsing sales in Ohio as part of the sales factor for apportioning corporation and trust income. In determining the situs of sales in Ohio for sales factor apportionment, the "cost of performance" standard is replaced with a "market-theory" approach based on where the taxpayer's customer enjoys the benefit of the taxpayer's sale.
2005	House Bill 66 launches a gradual phase-out of the 8.5 percent entity withholding tax rate for that portion of adjusted qualifying amounts pertaining to investors subject to the phase-out of the corporation franchise tax. The phase-out is complete in 2009.

Comparisons with Other States

(as of June, 2012)

The Ohio pass-through entity tax is a withholding tax on the distributive shares of income of qualifying investors.

The states with a tax most closely approximating the Ohio pass-through entity tax are those requiring withholding tax on the pass-through entity income of nonresident investors.

These states include **California, Illinois, Indiana, Kentucky, Massachusetts, Michigan, New Jersey, New York, Pennsylvania,** and **West Virginia.** This listing does not reflect taxes imposed by many states on certain types of income, such as the capital gains, built-in gains, and excess net passive income of "S" corporations, or any other type of entity-level tax.