

**SUMMARY OF PROPOSAL #30**  
*for consideration by the*  
**ARKANSAS TAX REFORM AND RELIEF LEGISLATIVE TASK FORCE**

**TOPIC: To Create a Deductible Pass-Through Entity Tax**

**Summary of Proposal for Consideration**

To amend the law regarding pass-through entities under Arkansas Code § 26-51-919 to allow a deductible business tax on pass-through businesses. This pass-through entity tax would provide affected business entities with favorable tax treatment in light of the cap on personal income tax deductions for state and local taxes (*i.e.*, SALT deduction) included in the federal Tax Cuts and Jobs Act (TCJA), effective for tax years beginning January 1, 2019.

**Fiscal Analysis**

According to the Department of Finance and Administration, fiscal analysis will depend on the specifics of the proposal and cannot be generalized at this time.

**Legal Analysis**

***Background***

Currently, Arkansas does not impose an entity-level tax on the income earned by a pass-through entity; rather, the income “passes through” to the individual owners and is subject to Arkansas income taxation at the individual level.

The TCJA limits the itemized deduction for state and local taxes to \$10,000. By limiting this deduction, owners of businesses operating in the pass-through entity form (*i.e.*, sole proprietorships, partnerships, limited liability companies, and S corporations) could see a rise in federal income taxes.

***Potential Legal Issues***

None.

***Other States***

- Iowa: Does not have a pass-through entity tax.
- Louisiana: Does not have a pass-through entity tax.
- Mississippi: Does not have a general pass-through entity tax; however, Mississippi does have a franchise tax that is imposed on S corporations. The franchise tax is computed based on the value of the capital employed or the assessed property values in the state. This tax will be phased out by tax year 2027. (MS St. §§ 27-13-5 and 27-13-8) Mississippi’s income tax laws allow for

a deduction for business expenses, including certain taxes paid. (Miss. Code Ann. § 27-7-17) It is unclear whether the franchise tax payments would qualify as a deductible business expense. This summary will be updated with any further information received from Mississippi.

- Missouri: Does not have a pass-through entity tax.
- Oklahoma: Does not have a deductible pass-through entity tax.
- Tennessee: Applies an excise tax of six and one-half percent (6.5%) on the net earnings of pass-through entities. (TN St. § 67-4-2007) Tennessee allows for taxpayers to take a credit against the excise tax for any individual income tax paid by the taxpayer. (TN St. § 67-4-2009)
- Texas: Does not have a deductible pass-through entity tax.