New Hampshire Entity Taxation Quirks and Conversions

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Kathryn H. Michaelis, Esq.  James Usseglio, CPA/PFS, MST
Rath Young Pignatelli  Baker Newman Noyes
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Agenda

• Overview and Challenges of New Hampshire Entity Level Taxation
• Business Profits Tax
• Business Enterprise Tax
• Interest and Dividends Tax
• Real Estate Transfer Tax
• Statutory Conversions
• Q&A
Knowing Our Audience...How Many of You:

- Regularly prepare NH tax returns?
- Have been involved in a NH tax audit?
- Have been involved in an entity conversion in NH?
- Have no idea what this topic is about?
New Hampshire Entity Level Taxation: Overview

• Business Profits Tax (BPT): Entity level apportioned net income tax on all business organizations
• Business Enterprise Tax (BET): Entity level apportioned tax on all business enterprises
• Real Estate Transfer Tax (RETT): Transfer tax imposed on transferor and transferee for transfers of real estate or interests in real estate holding companies
• Interest and Dividends Tax (I&D): Gross income tax on NH resident individuals, partnerships and LLCs represented by non-transferable shares
New Hampshire’s Tax System: What Makes Us Unique?

- No personal income tax
- No sales and use tax
- No corporate income tax / income tax on all “business organizations”
- Modified value added tax (BET)
New Hampshire Entity Level Taxation: Challenges

The look of an out-of-state tax practitioner looking to file in NH

- Unique tax system
- NH constitutional provisions
- Statutes and rules not always clear, often silent
- Limited case law and administrative guidance
- Instructions to tax forms
Business Profits Tax (BPT)

• “Business organizations” are subject to tax
• Filing threshold: > $50,000 gross business income
• The BPT does not adopt an organization’s federal tax classification – pass-through entities are subject to the BPT at the entity level
• Qualified Investment Companies (QICs) are exempt
• Combined unitary returns with water’s edge reporting required (interstate requirement)
BPT: Taxable Business Profits

• Gross business profits (specific federal taxable income starting points based on federal tax filing)
• +/- Adjustments
• Adjusted gross business profits
• NH apportionment (three-factor, double-weighted sales factor)
• Modified treatment of foreign dividends
• NH taxable business profits
• Credit against BPT for BET
Business Profits Tax: Quirks

What really goes on behind the scenes in crafting NH tax law?

- Business asset
- Separate entity adjustment
- Compensation deduction
- Step-up default & election
- Apportionment / Throwback
- DREs
- Combined unitary filings
- Qualified Investment Companies
- NOL deduction
Business Profits Tax: Simple…Right?

“I’m trying to simplify the IRC, you’re on your own in NH”

- Cancellation of debt income
- Charitable deduction limitations
- Capital loss limitations
- Tax attribute carryovers
- IRC Section 338(h)(10)
Business Profits Tax: Wait...There’s More?

• Distribution of appreciated property
• Tiered pass-through entities
• Sale of ownership interest in a business organization by a business organization
• Technical terminations
• Disguised sales
• Installment sales
• Taxation of foreign dividends
Business Enterprise Tax (BET)

- “Business enterprises” are subject to tax
- Filing threshold for 2017 tax year: > $208,000 of gross business receipts or > $104,000 of tax base
- Similar to BPT, pass-through entities are taxed
- Similar to BPT, QICs exempt
- Similar to BPT, grantor trusts included in return of owner
- Unlike BPT, combined reporting not permitted
- BET credit against BPT / 10 year carryforward
BET: Taxable Enterprise Value Tax Base

- Enterprise value tax base:
  - interest paid or accrued
  - dividends paid
  - compensation paid or accrued
- +/- Adjustments
- NH apportionment (each base separately)
- NH taxable enterprise value tax base
Business Enterprise Tax: Quirks

Yes, really, even the BET has quirks

- Dividends received deduction
- Employee leasing company election
- Capitalized interest
- Deferred compensation
- Gratuitous tips
- Self-employment earnings
- IRC Section 501(c) organizations
Interest and Dividends Tax (I&D)

• Tax base: interest and dividends (for PTEs, actual distributions, not allocations of income)
• Threshold: > $2,400 / $4,800 joint filers (exemptions)
• Taxpayers:
  • NH individual inhabitants or residents
  • Partnerships, LLCs and “associations,” the “beneficial interest in which is not represented by transferable shares” (NH ties)
  • Executors deriving appointment from a NH court
• NOT Taxpayers:
  • Trusts (NH grantors or beneficiaries are the taxpayers)
  • Corporations, partnerships and LLCs with transferable shares
  • Qualified Investment Companies (QICs)
Interest and Dividends Tax: Quirks

- Transferable versus non-transferable shares
- Subchapter S distributions
- Sale or exchange versus dividend treatment
- Single-member LLCs
- Definition of “gross income”
- Definition of LLC for I&D purposes – potential for tax benefit
Real Estate Transfer Tax (RETT)

• Taxable event: every “sale, granting and transfer” of real estate and “any interest therein”
  • Transfers of real estate
  • Transfers of interests in “real estate holding companies”
• Taxpayers: “buyer” and “seller”
• Tax rate: 1.5% on “price or consideration” (0.75% each on buyer and seller)
• Numerous exceptions
Real Estate Transfer Tax: Quirks

• Imposition of tax on transfers of interests in REHCs
• 2009-2012: controversial audits and court cases
• 2013-2016: legislative and regulatory clarity/reform
• Open issues remain:
  • REHC classifications
  • Reorganizations
  • Tiered structures
Statutory Conversions

- No BPT: no gain/loss recognition under 368(a)(1)(F)
- No BET: no distributions and BET credit carryover
- No RETT: no transfer under RSA 304-C:147
- No I&D: no dividend income to owners and LLC taxed at entity level

Quick Facts:
- IRC 368(a)(1)(F) reorganization
- Statutory conversion
- Same ownership %
- NH real estate owned
- Federal entity election effective as of date of conversion
- LLC has non-transferrable shares
- No other consideration
Statutory Conversions: Authority

• NH Corporate/LLC Law: RSA 304-C:147-149
• Federal Income Tax:
  • IRC §368(a)(1)(F) (“F” reorganization - mere change in form)
  • Treas. Reg. §301.7701-3 (check-the-box)
  • Rev. Rul. 64-250 (“S” election continues)
  • Rev. Rul. 73-526 (EIN continues)
• NH Tax:
  • RSA 77 (I&D Tax) and Rev 900s
  • RSA 77-A (BPT) and Rev 300s
  • RSA 77-E (BET) and Rev 2400s
  • RSA 78-B (RETT) and Rev 800s
  • New Hampshire Declaratory Ruling #10391
Statutory Conversions: Checklist

• Plan of conversion
• Business purpose for conversion
• Certificates of conversion and formation
• Cancellation of shares and issuance of “non-transferable” membership units
• LLC operating agreement (one class of stock and qualified “S” shareholders)
• IRS Form 8832 (entity classification election)
• IRS Form 2553 (confirmation purposes)
Contact Information

Kathryn H. Michaelis, Esq.
Rath, Young and Pignatelli, P.C.
One Capital Plaza
Concord, NH 03302
603-410-4303
khm@rathlaw.com

James Usseglio, CPA/PFS, MST
Baker Newman Noyes
650 Elm Street, Suite 302
Manchester, NH 03101
603-626-2237
jusseglio@bnncpa.com