



**TAX WEBINAR | DEC 13 AT 10AM**

**K2-K3 EXEMPTION NOTIFICATION PROCEDURES | COLORADO  
PASS-THROUGH ENTITY TAX (PTET)**

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# Agenda

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Brief SKR+CO overview



Year-end tax planning



K2/K3 domestic filing exception



Colorado PTET



Q+A

# Stockman Kast Ryan + Company

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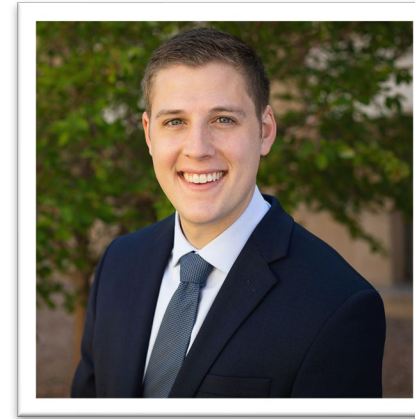
- Business + Individual Tax
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- Litigation Support
- Client Advising
- Business Valuations

# Today's Speakers

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**Jordan Empey, CPA**  
Tax Partner-in-Charge



**Grant Westerfield, CPA**  
Tax Manager





A photograph of two business professionals, a man and a woman, walking down a set of concrete stairs. The man is in the foreground, wearing a dark blue suit and brown leather shoes, carrying a black briefcase. The woman is behind him, wearing a light grey dress and black high heels, also carrying a black briefcase. The image has a blue overlay on the right side.

# Year-End Tax Planning

Jordan Empey, CPA

# Common Year-End Tax Planning Strategies

- Effective year-end tax planning considers each taxpayer's unique situation and tax planning goals.
- Tax Strategy when taxable income and rates remain consistent from year to year.
- Tax strategy when taxable income and rates are expected to decrease

1

Income deferral strategies

2

Deduction acceleration strategies

3

Expensing of capital assets (e.g., placing PP&E into service by Dec. 31, 2022)

4

Closing on taxable asset acquisitions before Dec. 31, 2022

# Reverse Tax Planning Strategies

Taxpayers should reverse traditional tax planning strategies if they expect to be in a higher income tax bracket in the following year. Common reverse tax planning strategies include:

- 1 Income acceleration strategies
- 2 Deduction deferral strategies
- 3 Capitalization of assets
- 4 Placing assets in service after Dec. 31, 2022
- 5 Closing on taxable acquisitions after Dec. 31, 2022

# Year-End Tax Planning

- 2022 Year-end Tax Planning Guides for businesses and individuals are available on our website.
- [www.skrco.com/webinars](http://www.skrco.com/webinars)

The flyer features the skr+co logo at the top left. Below it, a green banner reads 'TAX WEBINAR | DEC 13 AT 10AM'. A dark blue banner below that contains the title 'K2-K3 EXEMPTION NOTIFICATION PROCEDURES | COLORADO PASS-THROUGH ENTITY TAX (PTET)'. Underneath is a small circular photo of a man in a light blue shirt. The main title 'Year-End Tax Planning: K2-K3 Exemption Notification Procedures | Colorado Pass-Through Entity Tax (PTET)' is prominently displayed in the center. At the bottom, it says 'DECEMBER 13, 2022'. The footer includes 'CPAs + Business Advisors | skrco.com'.



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## 2022 Year-End Tax Planning for Businesses

U.S. businesses are facing pressure to drive revenue, manage costs and increase shareholder value, all while surrounded by economic and political uncertainties. Disruptions to supply chains brought about by the pandemic have continued into 2022. Inflation and rising interest rates have made the cost of debt, goods and services more expensive and cooled consumer spending. The stock market has declined sharply, and the prospect of a recession is on the rise. What's more, the outcomes of the upcoming November U.S. congressional elections — which as of the publication of this article are as yet unknown — will shape future tax policies. How do businesses thrive in uncertain times? By turning toward opportunity, which includes proactive tax planning. Tax planning is essential for U.S. businesses looking for ways to optimize cash flow while minimizing their total tax liability over the long term.

This article provides a checklist of areas where, with proper planning, businesses may be able to reduce or defer taxes over time. Unless otherwise noted, the information contained in this article is based on enacted tax laws and policies as of the publication date and is subject to change based on future legislative or tax policy changes.

### Recent legislative changes – the Inflation Reduction Act and the CHIPS Act

As the U.S. entered 2022, major proposed federal legislation that sought to raise taxes on large profitable corporations and high-income individuals (the Build Back Better Act) had died in the Senate. Although not nearly as broad in terms of tax increases, the Inflation Reduction Act (IRA) was enacted on August 16, 2022. Tax-related provisions in the IRA include:

- A 15% alternative minimum tax (AMT) on the adjusted financial statement income of certain large corporations (also referred to as the "book minimum tax" or "business minimum tax"), effective for tax years beginning after December 31, 2022.
- A 1% excise tax on corporate stock buybacks, which applies to repurchases made by public companies after December 31, 2022.
- Modification of many of the current energy-related tax credits and the introduction of significant new credits, including new monetization options.
- A two-year extension of the section 461(l) excess business loss limitation rules for noncorporate taxpayers, which are now set to expire for tax years beginning after 2028.

#### Corporate AMT

The AMT is 15% of the adjusted financial statement income (AFSI) of an applicable corporation less the corporation's AMT foreign tax credit. An applicable corporation is a corporation (other than an S corporation, a regulated investment company or a real estate investment trust) whose average annual AFSI exceeds \$1 billion for the prior consecutive three years. The AMT can also apply to a foreign-parented

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# Schedules K2/K3 Reporting Requirements

Jordan Empey, CPA

# Schedules K-2 and K-3 Reporting Requirements

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- The IRS introduced new Schedules K-2 and K-3 for the 2021 tax year
  - The new reporting requirements apply to partnerships, S corporations, and foreign partnerships
  - Trusts are **not** subject to the new reporting requirements
- Schedules K-2 and K-3 replace lines 16 and 20 on Schedules K and K-1 (Form 1065) and lines 14 and 17 of Schedule K and boxes 14 and 17 of Schedule K-1 (Form 1120-S)
- **Schedules K-2 and K-3 likely require more detailed information than partnerships and S corporations previously reported**

# Schedules K-2 and K-3 Reporting Requirements

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- Both Schedules K-2 and K-3 were created to standardize reporting of items of international tax significance to partners and shareholders
  - Prior to the 2021 tax year, Schedule K-1 only had a few boxes dedicated to foreign transactions and as a result, many taxpayers had to attach footnotes or additional statements to report the required information
  - Free-form footnotes and statements were often inconsistent and could result in incorrect reporting by the partner or shareholder
  - **Impetus for the change: Standardized schedules K-2 and K-3 reporting provides greater clarity and consistency to partners and shareholders**

# Schedules K-2 and K-3 Reporting Requirements

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- **Schedule K-2** is an extension of Schedule K and is used to report items of international tax relevance from the operation of the S corporation or partnership
  - The partnership or S corporation only files one Schedule K-2
- **Schedule K-3** is an extension of Schedule K-1 and is used to report the partner or shareholder's share of items reported on Schedule K-2
  - The partnership or S corporation files a separate Schedule K-3 for each partner or shareholder
- There are no general *de minimis* exceptions for filing the schedules

# Schedule K Changes

Foreign Transactions	<b>16a</b> Name of country or U.S. possession ▶			
	<b>b</b> Gross income from all sources . . . . .	<b>16b</b>		
	<b>c</b> Gross income sourced at partner level . . . . .	<b>16c</b>		
	Foreign gross income sourced at partnership level			
	<b>d</b> Reserved for future use ▶	<b>e</b> Foreign branch category . . . . . ▶	<b>16e</b>	
	<b>f</b> Passive category ▶	<b>g</b> General category ▶	<b>h</b> Other (attach statement) ▶	<b>16h</b>
	Deductions allocated and apportioned at partner level			
	<b>i</b> Interest expense ▶	<b>j</b> Other . . . . . ▶	<b>16j</b>	
	Deductions allocated and apportioned at partnership level to foreign source income			
	<b>k</b> Reserved for future use ▶	<b>l</b> Foreign branch category . . . . . ▶	<b>16l</b>	
	<b>m</b> Passive category ▶	<b>n</b> General category ▶	<b>o</b> Other (attach statement) ▶	<b>16o</b>
	<b>p</b> Total foreign taxes (check one): ▶ Paid <input type="checkbox"/> Accrued <input type="checkbox"/> . . . . .	<b>16p</b>		
	<b>q</b> Reduction in taxes available for credit (attach statement) . . . . .	<b>16q</b>		
<b>r</b> Other foreign tax information (attach statement)				



International Transactions	<b>16</b> Attach Schedule K-2 (Form 1065), Partners' Distributive Share Items-International, and check this box to indicate that you are reporting items of international tax relevance . . . . . <input type="checkbox"/>		
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# Schedule K changes, cont.

Final K-1       Amended K-1      651119  
 OMB No. 1545-0123

Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items			
1	Ordinary business income (loss)	15	Credits
2	Net rental real estate income (loss)		
3	Other net rental income (loss)	16	Foreign transactions
4a	Guaranteed payments for services		
4b	Guaranteed payments for capital		
4c	Total guaranteed payments		
5	Interest income		
6a	Ordinary dividends		
6b	Qualified dividends		



Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items			
1	Ordinary business income (loss)	14	Self-employment earnings (loss)
2	Net rental real estate income (loss)		
3	Other net rental income (loss)	15	Credits
4a	Guaranteed payments for services		
4b	Guaranteed payments for capital	16	Schedule K-3 is attached if checked . . . . . <input type="checkbox"/>
4c	Total guaranteed payments	17	Alternative minimum tax (AMT) items
5	Interest income		
6a	Ordinary dividends		
6b	Qualified dividends	18	Tax-exempt income and nondeductible expenses
6c	Dividend equivalents		
7	Royalties		
8	Net short-term capital gain (loss)		
9a	Net long-term capital gain (loss)	19	Distributions
9b	Collectibles (28%) gain (loss)		
9c	Unrecaptured section 1250 gain	20	Other information
10	Net section 1231 gain (loss)		
11	Other income (loss)		
12	Section 179 deduction	21	Foreign taxes paid or accrued

New checkbox for Schedule K-3

New line 21 – Foreign Taxes Paid or Accrued

# Schedules K-2 and K-3 Reporting Requirements

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- Partnerships and S corporations are only required to complete **relevant portions** of Schedules K-2 and K-3
  - Partnerships are **not required** to obtain information from their direct or indirect partners to determine whether they need to file certain parts of Schedules K-2 and K-3
  - S corporations are **not required** to obtain information from their shareholders to determine whether they need to file certain parts of Schedules K-2 and K-3



# Confusion around the Domestic Filing Exception



- In response to criticism from the tax practitioner community, the IRS is attempting to balance its need for foreign reporting information with the cost/benefit to pass-through entities and their stakeholders.
- The IRS released draft instructions in October 2022 that introduced a **domestic filing exception** that includes 4 criteria for eligibility.
- On Dec 2, 2022, the IRS released a ***revised draft instructions*** in an attempt to further clarifying the domestic filing exception instructions.

# Domestic Filing Exclusion – 4 Criteria

**Domestic Filing Exclusion:** A domestic partnership need not complete and file Schedules K-2 and K-3, nor furnish Schedule K-3 to a partner (except as specified), if the partnership meets four criteria for the tax year:

1. No or limited foreign activity.

2. U.S. citizens/resident alien partners.

3. Partner Notification

4. No 2022 Schedules K-3 requests by the 'one-month date.'

# First two criteria must be met to move on to 3 + 4

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## 1. No or limited foreign activity.

- Limited foreign activity refers to only passive foreign income with no more than \$300 of creditable taxes as indicated on payee/1099 statement.

## 2. U.S. citizens/resident alien partners.

- Also includes limited exceptions for decedent estates and trusts
- Dec 2 instructions added: S corporations with a sole shareholder, or (g) single-member LLCs where the LLC's sole member is one of the persons listed in (a) through (f) and the LLC is disregarded as an entity separate from its owner.



# Must then meet criteria #3 and #4

## 3. Partner Notification.

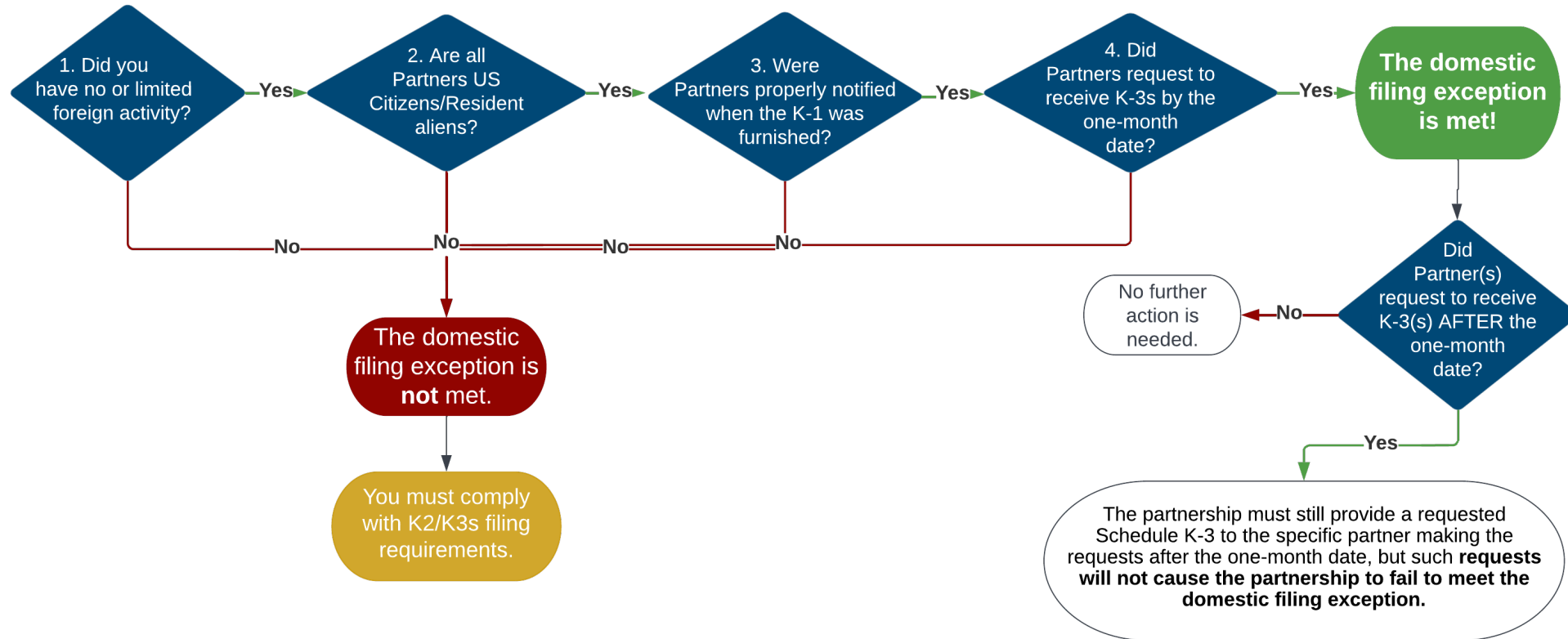
Partnerships satisfying the first two criteria must further:

- Notify their partners that they will not receive Schedule K-3 unless requested.
- **The notification must be made at the latest when the partnership furnishes the Schedule K-1 to the partner.**
- **The notice can be provided as an attachment to the Schedule K-1.**

## 4. No 2022 Schedules K-3 requests by the 'one-month date.'

- The partnership must not receive a request from any partner for Schedule K-3 information on or before the one-month date.
- **The “one-month date” is one month before the date the partnership files the Form 1065. For tax year 2022 calendar year partnerships, the latest one-month date is August 15, 2023, if the partnership files an extension.**
- The partnership must still provide a requested Schedule K-3 to partners making such requests after the one-month date, but such requests will not cause the partnership to fail to meet the domestic filing exception.

# What if someone requests a K2/K3?



## Notification and "1-month Date" details:

- Notify all partners that they will not receive Schedule K3s unless specifically requested.
- This notice may be included as an attachment when the K-1 is furnished.
- The request to receive K3 must be received "1-month" before filing the company's return (Form 1065)
  - Ex. If a company files a return on March 15, 2023, the "1-month date" would be February 15, 2023
- The latest "1-month date" is August 15, 2023, if the partnership files an extension.

# Example: Request rec'd before the one-month date

## Billings Company, Inc. ("The Company")

- ✓ Is a domestic partnership
- ✓ Has limited foreign activity
- Partners:
  - John and Jane Doe
    - U.S. Citizens
    - 40/40% ownership
    - Married
  - Al Sharp
    - U.S. Citizen
    - 20% ownership

- Al Sharp **requests Schedule K-3** from The Company for tax year 2022
- The Company receives this request on February 1, 2023.
- After requesting an extension, The Company **files** Form 1065 on **August 31, 2023**.
- The Company **does not qualify** for the domestic filing exception because Al Sharp requested the Schedule K-3 **before** the **1-month date (July 31, 2023)**.
  - As such, The Company must complete and file with the IRS the parts and sections of the Schedules K-2 and K-3 that are relevant to Al Sharp.
  - With respect to the Schedules K-2 and K-3 filed with the IRS, The Company does not need to complete, attach, or file any parts or sections relevant to John and Jane Doe, because they elected not to request them.
  - The Company must provide a copy of the filed Schedule K-3 to Al Sharp on the date that it files its return (Form 1065. )
  - The Company does not need to furnish a Schedule K-3 to John and Jane Doe.

# Example: Request rec'd after the one-month date

## Billings Company, Inc. ("The Company")

- ✓ Is a domestic partnership
- ✓ Has limited foreign activity
- Partners:
  - John and Jane Doe
    - U.S. Citizens
    - 40/40% ownership
    - Married
  - Al Sharp
    - U.S. Citizen
    - 20% ownership

- The Company receives a request from Al Sharp on **August 20, 2023**, (after the August 15, 2023 cut off date).
- The Company **qualifies for the domestic filing exception** because Al Sharp requested the Schedule K-3 after the 1-month date.
- The Company is **not required to file** the tax year 2022 Schedules K-2 and K-3 with the IRS **or furnish** the Schedule K-3 to the other owners, John and Jane Doe.
- However, The Company **is required to provide** the Schedule K-3, completed with the requested information, to Al Sharp on **September 20, 2023**, the later of the date on which The Company files the Form 1065 or 1 month from **August 20, 2023**.
- Because Al Sharp requested a Schedule K-3 for tax year 2022, the Company must file tax year 2023 Schedules K-2 and K3



# Colorado Pass Through Entity Tax (PTET)

Grant Westerfield, CPA



# Colorado enacts changes to pass-through entity tax

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- Colorado enacted an elective pass-through entity (PTE) tax regime, effective for tax years beginning January 1, 2022.
- On October 21, 2022, the Colorado Department of Revenue (DOR) released form [DR 1705](#) for making a Colorado PTE tax election **prior to the end of the 2022 tax year, on or before 12/31/2022.**
- Qualifying PTEs planning to make the election and take the state tax deduction on their federal return in the current tax year should consider making the election and payment prior to the end of the current tax period.
- Form DR 1705 is the election form for tax year 2022 providing taxpayers the ability to formally make the election by year end.

# Colorado PTET History

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- The Tax Cuts and Jobs Act (TCJA) of 2017 placed limits on state and local tax deduction for individual taxpayers, allowing only the first \$10,000 to be deducted
- Known as the “SALT cap,” this limitation mainly impacts high-income earners who itemize their deductions
- In 2021, Colorado enacted the “Salt Parity Act” to provide an elective PTE tax to provide a level of parity on the deductibility of state income taxes for C corporations and PTEs alike.
  - Allowed partnerships and S-corps to elect to pay Colorado income taxes on behalf of the owners at the entity level for Tax Years beginning Jan 1, 2022
  - This was later amended to allow for retroactive elections to include tax years 2018 – 2021; however, participating in this must occur on or after Sept 1, 2023 and before July 1, 2024\*

# PTET election for Tax Year 2022

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- Given the complexities of PTE elections, consider modeling the potential impact before making the election.
- Qualifying PTEs planning to make the election and take the state tax deduction on their federal return in the current tax year should make a payment prior to the end of the tax year.
- Form DR 1705 is the election form for tax year 2022 providing taxpayers the ability to formally make the election by year end.

# PTET election for future tax years

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- PTEs will be able to make the PTET election on their estimated payment forms.
- Form DR 1705 appears to only apply to the 2022 tax year.

# PTET Retroactive Elections

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- Colorado legislature adopted a retroactive election covering the 2018–2021 tax years
- The tax is imposed at the corporate income tax rate applicable to each of the tax years covered by the retroactive election—4.63% for 2018 and 2019, 4.55% for 2020, and 4.50% for 2021.
- The election to participate in the PTE tax regime on a retroactive basis must be made on or after Sep. 1, 2023, and before July 1, 2024.
- PTEs electing into the regime are required to file a composite amended tax return on behalf of all the PTE’s owners.
- Since FORM DR 1705 currently only applies to TY 2022, it should not be used for retroactive elections. Further departmental guidance and related forms are expected in fall of 2023.



# Question + Answer

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