

CHAPTER Rev 900 INTEREST AND DIVIDENDS TAX

PART Rev 901 DEFINITIONS

**Readopt with amendment Rev 901.01 through Rev 901.03 effective 8-10-04 (Doc 8137) to read as follows:**

Rev 901.01 "Accumulated profits" means:

(a) In the case of a corporation, other than a subchapter S corporation, the amount determined to be earnings and profits for federal income tax purposes; or

(b) In the case of all trusts represented by transferable shares, subchapter S corporations, limited liability companies, associations, and partnerships, the total undistributed revenues of the entity from whatever source derived.

Rev 901.02 A "beneficial interest in which is not represented by transferable shares", as used in RSA 77:3, I(b), means an interest in a trust:

(a) Where the equity interests are not transferable without obtaining prior beneficiary approval or causing a dissolution of the organization trust as authorized by the controlling trust document; and

(b) Which is not a:

- (1) Corporation;
- (2) Business trust;
- (3) Common law trust;
- (4) Massachusetts trust; or
- (5) Real estate investment trust.

Rev 901.03 A "beneficial interest in which is represented by transferable shares" means an interest in a trust:

(a) Which is a:

- (1) Business trust;
- (2) Common law trust;
- (3) Massachusetts trust; or
- (4) Real estate investment trust.

(b) Where property is placed in the hands of a trustee, who:

- (1) Acts apart from the beneficiaries; and

(2) Manages and deals with the property, as principal, for the use and benefit of the beneficiaries who hold equitable interests; and

(c) Where the equity interests are freely transferable without the necessity of securing prior beneficiary approval or causing a dissolution of the organization as authorized by the controlling trust document.

**Readopt with amendment Rev 901.05 effective 8-10-04 (Document 8137) to read as follows:**

Rev 901.05 "Corporation" means an artificial person or legal entity created under the laws of incorporation of any state or foreign country without recognizing the distinctions between types of corporations such as those drawn in the Internal Revenue Code of 1986 between S corporations and other corporations and shall also include organizations that are, for purposes of the federal income tax laws, taxed as corporations.

**Adopt Rev 901.06, and renumber Rev 901.06 as Rev 901.07, so that Rev 901.06 reads as follows:**

Rev 901.06 "Debt financed by the entity", as used in RSA 77:1-a, II(c), means liabilities incurred by the entity that allow a distribution to be made to the owners of an entity, but only to the extent that the distribution would be considered to be a deemed dividend under Rev. 903.05 or Rev. 903.01.

**Readopt with amendment Rev 901.07 and renumber as Rev. 901.08 effective 8-10-04 (Doc 8137) to read as follows and renumber Rev 901.08 as Rev 901.09:**

Rev 901.08 "Dividends" means "dividends" as defined in RSA 77:1-a, II, namely "an amount of property distributed, with respect to their ownership interest, other than in liquidation of the organization, to shareholders or interest-holders of an organization from:

- (a) Current year profit;
- (b) Accumulated profits of such entity; or
- (c) Debt financed by the entity."

**Adopt Rev 901.10 as follows and renumber Rev 901.10 through 901.11 as Rev 901.12 through Rev 901.13:**

Rev 901.10 "Entity" means, as used in RSA 77:1-a,II(c), an organization, as defined in Rev. 901.15.

**Adopt Rev 901.14 as follows:**

Rev 901.14 "Internal Revenue Code (IRC)" means the United States Internal Revenue Code of 1986, as amended.

**Readopt and renumber Rev 901.12 as Rev 901.15, eff. 8-10-04 (Doc 8137) as follows and renumber Rev 901.13 through 901.16 as Rev 901.16 through Rev 901.19:**

Rev 901.15 "Organization" means:

- (a) A corporation;
- (b) A business trust;
- (c) An estate;
- (d) A trust;
- (e) A partnership;
- (f) An association;
- (g) Two or more persons having a joint or common business interest;
- (h) Limited liability company; or
- (i) Any other legal or commercial form of business.

**Adopt Rev 901.20 as follows:**

Rev 901.20 "Total undistributed revenues" means, in the case of an organization required to file a federal partnership return or a limited liability company required to file as a proprietorship, the excess income received and retained by an organization after the payment of its expenses from the current tax year or from prior tax years.

**Readopt with amendment Rev 901.17 effective 8-10-04 (Doc # 8137) and renumber as Rev 901.21 to read as follows:**

Rev 901.21 "Transferable" as used in RSA 77:3,I(b) means the ability of a shareholder or interest holder in an organization to dispose of, by any means, all rights incidental to his or her equitable interest without a required approval of the disposition by another beneficiary, and without dissolution of the organization itself.

**Repeal Rev 901.18 effective 8-10-04 (Document # 8137) as follows:**

~~Rev 901.18 "Usual place of business" as used in RSA 77:14 and 16 means the primary place of business or a regularly used place of business of an organization.~~

**PART Rev 902 RESIDENCY AND TAXABILITY OF SPECIAL ENTITIES:**

**Readopt with amendment Rev 902.06 through Rev 902.09 effective 8-10-04 (Doc.# 8137) to read as**

**follows**

## Rev 902.06 Mutual Funds

(a) Mutual funds shall be presumed to be organizations incorporated under the laws of New Hampshire or some other state of the United States;

(b) Mutual funds shall not be required to:

- (1) File a return;
- (2) Pay a tax; or
- (3) Use the allocation of income provisions of RSA 77:12.

(c) Investors in mutual funds shall be taxable if they are:

- (1) New Hampshire residents;
- (2) Trusts within the scope of RSA 77:3, I(b); or
- (3) Fiduciaries, deriving their appointment from a court of this state within the scope of RSA 77:3, I(c).

(d) Amounts received from such funds by investors on all investments shall be taxable dividends except for:

- (1) New Hampshire direct or municipal obligations; and
- (2) Direct obligations of the United States Government.

(e) Amounts received from such funds by investors on all investments in New Hampshire direct or municipal obligations and direct obligations of the United States Government shall be deemed to be an investment by the investor in such New Hampshire direct or municipal obligations and United States Government obligations and not be considered taxable dividends.

(f) Investors receiving distributions from mutual funds that invest in New Hampshire direct or municipal obligations and direct United States obligations and other types of investments shall not include as taxable dividends any amount:

- (1) Reported to the investor by the mutual fund as interest from New Hampshire direct or municipal obligations and direct obligations of the United States Government;
- (2) Determined by multiplying the total amount received by a fraction:
  - a. The numerator of which shall be the amount of interest on New Hampshire direct or municipal obligations and direct obligations of the United States Government received by the mutual fund; and
  - b. The denominator of which shall be the total amount of income received by the mutual

fund from all activities; or

(3) Determined by multiplying the total amount received by the mutual fund's percentage of assets invested in New Hampshire direct or municipal obligations and direct obligations of the United States Government.

Rev 902.07 Trusts.

(a) The interest and dividends tax shall be applied at the:

(1) Entity level for trusts when:

- a. The entity has a usual place of business within New Hampshire or the trust property is located in New Hampshire;
- b. Any trustee, owner or beneficiary is an inhabitant or resident of New Hampshire; and
- c. The equitable interest is not represented by transferable shares; or

(2) Owner or beneficiary level for trusts when:

- a. The entity does not have a usual place of business within New Hampshire or the trust property is located outside of New Hampshire;
- b. One or more of the trustees, owners or beneficiaries are inhabitants or residents of New Hampshire; and
- c. The-equitable interest is not represented by transferable shares.

(b) The amount of taxable interest and dividend income shall be determined as follows:

(1) All interest and dividends received, which would be taxable if received by a resident individual, shall be taxable to a trust if:

- a. The beneficial interest of the trust is composed of non-transferable shares;
- b. The location of the trust property is in New Hampshire; and
- c. All of the trust's interest holders are residents or inhabitants of New Hampshire; or

(2) A pro-rata portion of the interest and dividends received, which would be taxable if received by a resident individual, shall be taxable to a trust if:

- a. The beneficial interest of the trust is composed of nontransferable shares;
- b. The trust property is in New Hampshire or the trustee has derived his or her appointment from courts of New Hampshire; and
- c. Some of the trust's interest holders are residents or inhabitants of New Hampshire; or

(3) When a partnership, LLC, association or trust is not taxable as an entity and it has beneficial interests composed of non-transferable shares with some interest holders being residents or inhabitants of New Hampshire, then:

- a. The interest and dividend income subject to tax shall be:
  1. Reported by the resident interest holders; and
  2. Imposed on the portion of the distribution which represents interest or dividends received by the entity; and
- b. The portion of the distribution shall be determined by multiplying the amount of the actual distribution received by a fraction:
  1. The numerator of which shall be the total interest and dividend income received by the entity; and
  2. The denominator of which shall be the total amount of gross income received by the entity.

Rev 902.08 Accounting Method For Determination of Accumulated Profits.

(a) A corporation, including an S corporation, shall compute the amount of its accumulated profits in conformity with the provisions of the Internal Revenue Code of 1986, as amended for the calculation of earnings and profits.

(b) Trusts composed of transferable shares, may elect to continuously calculate its accumulated profits in a manner:

- (1) Consistent with the calculation of corporate earnings and profits under the Internal Revenue Code of 1986, as amended or
- (2) Which conforms in all respects to generally accepted accounting principles.

(c) The trust shall maintain records showing:

- (1) The method selected in (b) above; and
- (2) The calculation of the current year and accumulated profits

(d) The partner or member of an organization required to file a federal income tax return as a partnership shall compute ~~its~~ accumulated profits attributable to the partner or member in the following manner:

- (1) The calculation of current year profits shall be determined at the individual partner or member level based on information provided on the federal form 1065, schedule K-1 and shall be the summation of the following items:

a. The following items of income or gain shall be added and losses subtracted:

1. Ordinary business income or loss;
2. Net rental real estate income or loss;
3. Other net rental income or loss;
4. Interest income;
5. Ordinary dividends;
6. Royalties;
7. Net short-term capital gain or loss;
8. Net long-term capital gain or loss;
9. Collectibles gain or loss;
10. Unrecaptured Section 1250 gain;
11. Net Section 1231 gain or loss;
12. Other income or loss; and,
13. Net of tax-exempt income and non-deductible expenses.

b. The amount of the IRC Section 179 deduction shall be subtracted, or if records are available, the amount of IRC Section 179 deduction may be converted to straight-line depreciation amortized over the life of the assets for which the IRC Section 179 deduction is taken;

c. Gain that was not recognized by the organization for federal income tax purposes on property distributed to the partner or member shall be added, but only if such gain would have been recognized by the organization on such distribution if the organization were considered a subchapter C corporation under the IRC;

d. The amount of compensation that would be deductible for those services provided by the member or partner under RSA 77-A:4, III if the entity were subject to the tax imposed under RSA 77-A in the year that the compensation for services would be deductible, less the amount received by the partner or member as guaranteed payments for service, shall be subtracted. A payment of unpaid compensation from a prior year shall not decrease accumulated profits.

(2) The net of the current year profits and the distributions made during the year from current year profits shall be an addition to accumulated profits from prior years.

(3) If distributions made during the year exceeds current year profits, the amount of distributions that exceeds current year profits shall reduce accumulated profits to the extent the organization has positive accumulated profits.

(e) A limited liability company required to file a return as a proprietorship shall compute its accumulated profits in the following manner:

(1) The calculation of current year profits shall be the summation of the following items;

a. The following items of income or gain shall be added and losses subtracted:

1. Net profit or loss from a business or profession;
2. Net rental real estate income or loss;

3. Other net rental income or loss;
4. Interest income;
5. Ordinary dividends;
6. Royalties;
7. Net short-term capital gain or loss;
8. Net long-term capital gain or loss;
9. Net IRC Section 1231 gain or loss;
10. Other income or loss; and,
11. Net of tax-exempt income and non-deductible expenses.

b. Reduced by the amount of compensation deduction taken by the organization under RSA 77-A:4, III, attributable to the personal services of the member. A payment of unpaid compensation from a prior year shall not decrease accumulated profits.

(2) The net of the current year profits and the distributions made during the year from current year profits shall be an addition to accumulated profits from prior years.

(3) If distributions made during the year exceeds current year profits, the amount of distributions that exceeds current year profits shall reduce accumulated profits to the extent the organization has positive accumulated profits.

(f) If an organization, partner or member does not maintain records showing the calculation of accumulated profits, and a distribution is made to the shareholders, interest holders, partners or members the department shall presume there are adequate accumulated profits to treat the distribution as a dividend.

(g) The determination of whether a distribution was made from accumulated profits shall occur as of the last day of the tax year and not the date of distribution.

(h) A taxpayer owning an interest in an organization required to file a federal income tax return as a partnership, limited liability company required to file as a proprietorship, or other organization the distributions of which became taxable pursuant to Chapter Law 144:275-280, Laws of 2009, shall compute its accumulated profits from the later of the following tax years:

(1) The first tax year the taxpayer owned an interest in the organization; or

(2) From the beginning of tax years ending on or after December 31, 2009 provided however, the taxpayer may elect to compute the accumulated profits of the organization from the inception of the organization.

Rev 902.09 Mixed-ShareTrusts With respect to trusts composed of a mixture of share types, the tax status of such organizations and the holders of equity interests in such organizations, shall be determined as follows:

(a) When the majority of the outstanding equity interest in the entity is composed of transferable shares:

(1) Each share shall be deemed a transferable share;



- (2) The trust shall not be subject to tax under RSA 77; and
  - (3) The distributions of profits to any equity interest holder shall be considered a dividend subject to the interest and dividends tax; or
- (b) When the majority of the outstanding equity interest in the trust is composed of non-transferable shares:
- (1) Each share shall be deemed a non-transferable share;
  - (2) The trust shall be subject to tax under RSA 77; and
  - (3) The distribution of profits to any equity interest holder shall not be considered a dividend subject to the interest and dividends tax.

Source. #6321, eff 8-22-96; ss by #8137, eff 8-10-04

#### PART Rev 903 INCLUSIONS AND EXCLUSIONS TO INCOME

##### **Readopt with amendment Rev 903.05 effective 8-10-04 (Doc.# 8137) to read as follows:**

Rev 903.05 Deemed Dividends With the exception of distributions in liquidation, the following transactions between an organization and its shareholders or interest-holders shall be considered a dividend:

- (a) All property transferred from an organization to a shareholder or interest-holder with respect to the shareholder's or interest-holder's ownership interest from the accumulated profits of the organization;
- (b) All personal expenditures made by an organization on behalf of a shareholder or interest-holder which have not been properly reported as compensation or loans for federal income tax purposes;
- (c) Forgiveness of a shareholder or interest-holder's indebtedness to the organization;
- (d) The automatic re-investment of property distributed from current year's or accumulated profits into additional stock; and
- (e) A distribution purported to be a loan or advance to an interest-holder by the entity is such that pursuant to under IRC § 316 the distribution is a dividend. In determining whether a distribution purported to be a loan or advance is a dividend under IRC § 316 the commissioner and taxpayer may consider relevant federal court decisions.

##### **Readopt with amendment Rev 903.06, eff. 8-10-04 (Doc 8137) to read as follows:**

Rev 903.06 Sequence of Distributions. All actual distributions shall be presumed to be sequentially made from:

- (a) Unpaid compensation deduction allowable under RSA 77-A:4,III to a partner or member;
- (b) The current year profit of the organization;

- (c) The organization's accumulated profits; and
- (d) The capital of the organization.

**Adopt Rev 903.07 as follows, and renumber 903.07 and Rev 903.08 as Rev 903.08 and 903.09**

Rev 903.07 Guaranteed Payments For Use of Capital.

(a) A guaranteed payment for the use of an owner's capital, and received by a New Hampshire resident from an entity taxed as a partnership for federal income tax purposes shall be considered interest for purposes of RSA 77.

(b) Any other guaranteed payment shall not be considered to be a taxable dividend to the extent that the entity would be entitled to a deduction for the personal services of the New Hampshire resident under RSA 77-A:4, III.

Adopt Rev 903.10 and Rev 903.11 as follows:

Rev 903.10 Distribution as Compensation For Services Provided. A non-liquidating distribution received by a New Hampshire resident who is an owner of an organization required to file a federal return as a partnership or proprietorship shall not be subject to RSA 77 to the extent that the services provided by the New Hampshire resident would allow the entity making the distribution a deduction for personal services under RSA 77-A:4,III, if the entity was subject to the tax imposed under RSA 77-A.

Rev 903.11 Support for Claim on Non-Taxable Distribution. A distribution received by a New Hampshire resident from an organization that is required to file a federal income tax return as a partnership or a limited liability company filing a federal return as a proprietorship shall be presumed to be subject to RSA 77 unless the New Hampshire resident is able to demonstrate that the distribution was either:

- (a) For personal services provided by the New Hampshire resident for which the entity did, or would have received a deduction under RSA 77-A:4,III, if it had been required to file a return under RSA 77-A;
- (b) A return of capital, or
- (c) A liquidating distribution.

## APPENDIX A – Examples

**Rev 901.20 “Total undistributed revenues”****EXAMPLE 1: Compensation Deduction Reduces Accumulated Profits**

Two NH residents each own 25% interests in an LLC, while a corporation owns the other 50%. The only activity of the LLC is the rental of real estate. It has net income from real estate activities of \$200K in its first year of operation. One of the NH residents provides no services to the LLC. The other resident and the corporation each provide services to the LLC that would be worth \$40K if paid to an unrelated employee on an arm’s length basis. The LLC makes non-liquidating distributions of \$50K to each of its two resident members and \$100K to the corporation. Since the corporation is not a natural person, the LLC would not be allowed any deduction for personal services under RSA 77-A:4, III for work performed on its behalf by the corporation. The LLC would, however, be allowed a \$40K deduction for the personal services of the one resident member, who is a natural person.

None of the \$100K received by the corporation is subject to I&D tax since corporation are exempt from the tax. The resident member of the LLC who performed services would have a taxable dividend of \$10K (with the other \$40K received considered compensation, which is not subject to I&D.) The resident member who did not perform services would have a taxable dividend equal to the entire \$50K distribution received.

**EXAMPLE 2: Compensation Deduction Applies Only to Accumulated Profits of Services Partner**

Same facts as the example above but the services provided by the NH resident member are worth \$60K, instead of \$40K. Despite the fact that the LLC would have a \$60K compensation deduction for BPT purposes, that additional compensation deduction does not reduce the amount of accumulated profits for the other members.

**EXAMPLE 3: Guaranteed Payments Reduces Compensation Deduction Applied Against Accumulated Profits:**

A partnership has two partners, each of whom is a NH resident and owns a 50% share of the partnership. Each partner is guaranteed a payment of \$10K for services rendered. In its first year of operation, the partnership has \$100K of income from trade or business, and each partner performs services that would be worth \$30K if paid to an unrelated person on an arm’s length basis. The accumulated profits attributed to each partner prior to any distributions would be \$30K, as demonstrated by the following calculation:

Income from Trade or Business	100,000
Partnership Share	<u>50%</u>
Income from Trade/Business Before Comp Deduction	50,000
Value of Services Rendered	30,000
Less Guaranteed Payment for Services*	<u>10,000</u>
Personal Comp Deduction Applied Against Accumulated Profits	<u>20,000</u>
Accumulated Profits	30,000

\*The guaranteed payments for services were already deducted to arrive at the amount of Income from Trade or Business.

If the partnership paid a distribution of \$50K to each partner, they would each have to report taxable dividends for I&D purposes of \$30K, the amount of the accumulated profits attributable to them.

**Rev 902.08 Accounting Method For Determination of Accumulated Profits.**

EXAMPLE 1: Distribution of Appreciated Property to Owners: Assume an LLC has no accumulated profits, but the fair market value of its real estate has appreciated since acquisition by \$1M. At year end the LLC distributes equal tenants-in-common interests in the property to its two NH-resident members. The members each have \$500K of taxable dividends for I&D purposes (which is equal to the fair market value of the asset less its basis.) This treatment parallels the taxability of distributions of appreciated property from a corporation.

EXAMPLE 2: Distribution of Asset That Declined in Value – LLC Has Accumulated Profits Assume an LLC has \$200K of accumulated profits and the fair market value of land it bought for \$400K has declined in value since acquisition by \$100K. At year end the LLC distributes equal tenants-in-common interests in the property to its two NH-resident members. Even though the fair market value of the property distributed was \$300K, for I&D purposes the members have a taxable distribution of \$200K, which is the amount of accumulated profits of the LLC at the time of distribution. This treatment parallels what would happen with a distribution of property that declined in value from a corporation.

EXAMPLE 3: Distribution of Asset That Declined in Value – LLC Has No Accumulated Profits: Assume the same facts in the example above with the exception that the LLC has no accumulated profits. At year end the LLC distributes equal tenants-in-common interests in the property to its two NH-resident members. The members have not received a taxable distribution for I&D purposes because the LLC has no accumulated profits. This treatment parallels what would happen with a distribution of property that declined in value from a corporation.

**EXAMPLE 4: Tax-Exempt Income Is Included in Accumulated Profits**

A partnership has two NH residents as partners, each of whom owns a 50% interest. The only source of income for a partnership during its existence has been interest on Portsmouth municipal bonds, which is tax exempt for income tax purposes. It makes a non-liquidating distribution of \$50K to each partner. Since tax-exempt income would be included in the earnings and profits of a C corporation, it is also includible in the total undistributed revenues and accumulated profits of a partnership. Each partner would have \$50K of taxable dividend income for I&D purposes.

**EXAMPLE 5: Section 179 Deduction Amortized Over 5 Years for Accumulated Profits**

An accrual-basis LLC is owned 50-50 by two NH residents. The LLC, which has elected to be treated as a partnership for federal tax purposes, has \$100K of ordinary income from a trade or business in its first year of operation. In arriving at that \$100K of ordinary income, it took a \$50K deduction under IRC Sec. 179. The LLC made non-liquidating distributions of \$60K to each of its two members during the year. Since Sec. 179 deductions are amortized over five years in calculating earnings and profits, the entire \$120K in distributions would be taxable for I&D purposes.

Calculation of Accumulated Profits	
Ordinary Income from Trade or Business	100,000
Add Back Sec. 179 Deduction	50,000
Less Sec. 179 Deduction Allowable in Yr 1	<u>10,000</u>
Sec. 179 Deduction Not Allowable in Yr. 1	<u>40,000</u>
Accumulated Profits Before Distribution	140,000

Taxable Distributions for I&amp;D Purposes

120,000

Rev 903.05 Deemed Dividend

EXAMPLE 1: An LLC that began business on Jan. 1, 2010 had \$50K of current-year profits. The LLC's federal tax return indicated that no distributions were made to its sole member, a NH resident, during 2010. The member, who did not perform personal services for the LLC, took \$30K in cash out of the entity during the year. The LLC's balance sheet included with its federal return showed a \$30K loan to its members. The LLC also paid \$20K of his personal expenses. There was no formal loan agreement signed and the member did not pay interest on either the cash received or the personal expenses paid by the entity. The member would have a taxable deemed dividend of \$50K, which is equal to the amount of the LLC's current-year profits.

RULE	STATUTE
Rev 901.01	RSA 77-A:4
Rev 901.02	RSA 77:3, I(b)
Rev 901.03	RSA 77:4, III
Rev 901.05	RSA 21-J:13,I
Rev 901.06 New	RSA 21-J:13,I
Rev 901.07	RSA 77-A:4, RSA 77:1-a,II(c)
Rev 901.08	RSA 77-A:4
Rev 901.09	RSA 21-J:13,I, RSA 77:1-a,II(c)
Rev 901.10 New	RSA 77-A:1-a,II(c)
Rev 901.11-901.13	RSA 21-J:13,I
Rev 901.14 New	RSA 21-J:13,I
Rev 901.15	RSA 21-J:13,I, RSA 77:5
Rev 901.16-901.19	RSA 21-J:13,I
Rev 901.20 New	RSA 21-J:13,I
Rev 901.21	RSA 21-J:13,I
Rev 902.06 amended	RSA 21-J:13,I, RSA 77:12
Rev 902.07 amended	RSA 21-J:13,I, RSA 77-A:4
Rev 902.08 amended	RSA 21-J:13,I
Rev 902.09 amended	RSA 21-J:13,I
Rev 903.05 amended	RSA 21-J:13,I, RSA 77-A:4
Rev 903.06 New	RSA 21-J:13,I
Rev 903.07 New	RSA 21-J:13,I
Rev 903.10 New	RSA 21-J:13,I
Rev 903.11 New	RSA 21-J:13,I