

Daily Tax Report: State

# SALT Cap Workarounds May Catch On in More States After IRS OK

By Sam McQuillan

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- IRS announced rules that approve a path around SALT cap
  - \$10,000 deduction cap opposed in high-tax states
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More states are expected to pass laws letting businesses avoid the limit on personal tax deductions for state and local taxes, following IRS guidance approving the workaround.

Already, states including New Jersey and Connecticut softened the blow of the \$10,000 SALT cap with provisions for pass-through businesses like partnerships and S corporations, which are taxed normally at the owner level.

The IRS said Monday in a notice that forthcoming proposed rules will allow the states' workaround, which involves an entity-level tax that is offset by a corresponding individual income tax credit.

"Now that the uncertainty has been removed, you are going to see more states enact some form of pass-through entity tax," said Marc Finer, a Hartford, Conn.-based tax attorney at Murtha Cullina LLP, who warned last year that benefits from Connecticut's workaround could be short-lived because of uncertainty about how the IRS would treat it.

Connecticut's workaround law is mandatory, so partners or shareholders have no control over whether they keep pass-through status.

The SALT cap was a politically fraught element of the 2017 Republican tax law, and is generally opposed by Democrats in high-tax states.

Bruce Ely, a partner at Bradley Arant Boult Cummings LLP in Birmingham, Ala., estimated that as many as four more states could enact workarounds in upcoming legislative sessions. He expects Alabama to introduce a bill when its Legislature meets in February.

"Right now I'm going to go back to my legislators and show them this notice," Ely said. "There is no concern now about the validity of these taxes."

**'A Lot' of Relief**

Connecticut became the first state to enact the workaround in 2018. Since then tax advisers have generally been viewing the IRS's silence as acquiescence.

"I am very curious why it took them three years to push something out," said Albert J. Campo, a CPA and managing partner at AJC Accounting Services in New Jersey.

The agency in 2019 killed off (T.D. 9864) a different workaround some states tried, which would have allowed state tax credits for donations made to charitable funds.

The timing of Monday's notice could have been part of the government's effort to bring small businesses relief during the Covid-19 pandemic, said Amie Kuntz, a CPA with RubinBrown in Iowa.

"This is relief to a lot of people. There are a lot of small business owners and the amount of partnerships and S corporations there are is just enormous," she said.

To contact the reporter on this story: Sam McQuillan in Washington at [smcquillan@bloomberglaw.com](mailto:smcquillan@bloomberglaw.com)

To contact the editors responsible for this story: Jeff Harrington at [jharrington@bloombergtax.com](mailto:jharrington@bloombergtax.com); Colleen Murphy at [cmurphy@bloombergtax.com](mailto:cmurphy@bloombergtax.com)

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