

More SALT Workarounds Ahead as States Add Pass-Through Tax

By Annie Goulart and Laura Holt 2023-04-28T13:46:50000-04:00

- In., Ky., Mt., W.Va. latest to eye SALT bypass
- Future of SALT cap workarounds an open question

Differences in the application of extensions, retroactivity, estimated payments, and credits remain the key elements that practitioners must navigate when dealing with the varying approaches to pass-through entity taxes.

Indiana, Kentucky and West Virginia are the most recent states to enact legislation to reduce the effect of the 2017 \$10,000 SALT cap deduction limitation for individuals who conduct business through a pass-through entity.

“PTE owners and their tax advisors need to carefully model the tax implications of electing into one or more of these PTE taxes, because they can have unanticipated consequences depending on the entity’s business footprint, the nuances of each state’s tax, and the availability of credits to the entity’s ultimate owners in their states of residence for entity taxes paid,” Kelvin Lawrence, partner at Dinsmore & Shohl, LLP in Columbus, Ohio, and member of Bloomberg Tax’s State Tax Advisory Board, said in an email.

While new or proposed laws in Indiana, Kentucky, Montana, and West Virginia are similar, they differ in key respects regarding elections and credits. To make an election, Kentucky and Indiana allow the election to be made by an “authorized person.” Montana would require the entity to designate a representative to make the election. West Virginia has not issued specifics regarding who can make the election for the pass-through entity, but we anticipate more details will be released in the coming weeks. With regard to credits, Kentucky, Montana, and Indiana’s credit for taxes paid is refundable to the pass-through entity owner, whereas credit in West Virginia is nonrefundable. West Virginia allows excess credit to be carried forward for up to five taxable years.

Elections & Extensions: The timing of PTE elections may have significant tax implications for owners filing individual income tax returns with a normal due date of April 18, 2023. Owners may be overstating their share of PTE income unless they wait for the PTE to make the election and issue the

owner's K-1 after the election is made. As a result, practitioners should consider whether such individuals would be best served by extending their individual income tax return to allow PTEs time to make the election and provide owners with the information necessary to claim a credit for their share of taxes paid at the entity level.

Retroactivity: Many states, including [Indiana](#), Kentucky, and West Virginia allow pass-through entities to make a tax election to apply retroactively to tax year 2022. Since due dates and election methods vary by state, practitioners must be aware of multiple [deadlines](#). For entities required to file returns by March 15, the timing of enactment for SALT cap workarounds created this year may require filing an extension or amended return. It is important to note that Massachusetts and New Jersey do not allow elections on an amended return.

Estimated payments: Most states allowing PTE entity level taxes require that the electing entity make [estimated payments](#) for tax years beginning in 2023 (several states waive the estimated payments for tax years 2021 and 2022). Missouri and Idaho do not require estimated payments and Utah and Virginia have not yet released guidance. Taxpayers should pay close attention to whether [failure to make estimated payments affects election eligibility](#).

Owner level credits: Most states allow an owner level credit in the amount of the PTE tax paid against individual income tax; however, Kentucky's legislation initially limited the credit to 95% of tax paid but was amended before enactment to allow for a credit equal to 100% of tax paid.

Indiana's credits are refundable to the taxpayer, whereas West Virginia allows any excess credit to carry forward for up to five additional tax years.

Additionally, several states allow taxpayers to claim a [credit for taxes paid to another state](#).

However, this uncertainty hasn't deterred states from continuing to introduce legislation that would enact a PTE tax. If legislation is enacted, Hawaii, Iowa, Montana, and Vermont would join more than 30 states with PTE taxes.

"We can expect PTE taxes to continue to spread and to be a part of the state tax landscape for as long as the limitation on the SALT deduction lasts – possibly longer," Lawrence said.

Will Congress Act?

With a divided Congress, it is unlikely that consensus will be reached on [repealing](#), extending, or changing the cap. Republican members of Congress proposed [extending and raising the cap](#), while numerous Democrats continue to rail against the cap and many favor allowing its expiration. The House's bipartisan [SALT Caucus reconvened](#) to discuss an end to the current cap and the prevention of a future extension, but little progress was made.

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