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IRS to Crackdown on SALT Deduction Cap Workarounds.

On May 23, 2018, the IRS and the Treasury Department issued [Notice 2018-54](#) announcing their intention to propose regulations addressing the federal tax treatment of state workarounds to the \$10,000 (\$5,000 in the case of married individuals filing separately) state and local tax deduction limitation (SALT Cap) under IRC section 164 as revised by the Tax Cuts and Jobs Act. The regulations will address certain state responses to the SALT Cap, which offers taxpayers an option to contribute to state or local controlled funds in exchange for credits against state or local tax obligations. These state responses to the SALT Cap are intended to provide taxpayers with a deductible charitable contribution in lieu of state and local tax payments, the deduction of which would be limited under the SALT Cap. The regulations will emphasize that federal income tax substance-over-form principles, not state laws, dictate the determination of whether a payment is a charitable contribution or is otherwise deductible for federal income tax purposes.

New York (S.B. 7509), New Jersey (S.B. 1893), and Connecticut (Subst. S.B. 11) already have enacted workaround legislation intended to allow taxpayers to claim a federal tax deduction for payments that exceed the SALT Cap. New Jersey, for example, has authorized its municipalities, school districts, and counties to create charitable funds that grant contributors property tax credits for up to ninety percent of their payments. New York offers a similar arrangement, offering tax credits for payments to state charitable funds, up to eight-five percent of the amount of such contributions in the case of state income taxes and up to ninety-five percent for local property taxes. Other states such as California (S.B. 227) and Illinois (H.B. 4237) have introduced similar bills allowing tax credits for charitable contributions. The California bill passed in the Senate and is held up in the Assembly, while the Illinois bill passed in the House and its third reading in the Senate is scheduled for today, May 24, 2018.

A key question the impending regulations will likely address, given the Notice's mention of substance-over-form principles and a reference to the federal charitable contribution deduction, is the charitable intent of the taxpayer. IRC section 170 provides that a taxpayer may deduct any "charitable contribution," defined generally as a contribution or gift to or for the use of qualifying entities, from taxable income. Such contributions must be made voluntarily and with donative intent. If the taxpayer is making the contribution in order to obtain the credits, the donative intent may not be present. Additionally, if a taxpayer receives a benefit for a charitable contribution, the related deduction is generally limited to the amount that the transfer surpasses the fair market value of the benefit received. Hence, workaround contributions in New Jersey, as noted above, would be limited to a ten percent deduction.

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USA May 24 2018

