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Law Alert

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New California Law Allows SALT Work-around

On July 16, 2021, California enacted AB 150 which dealt a significant blow to the 2017 federal tax law which limited the itemized deduction for state and local taxes [SALT] to \$10,000. Two provisions of AB 150 make this so: newly added Revenue and Taxation Code sections 17052.10 and 19900-19906.

Sections 19900-19906 provide for an optional tax paid by pass-through entities such as partnerships, limited liability companies and S corporations. The tax is set at 9.3%. [Other taxes and fees on such entities will continue to apply, such as the 1.5% tax on S corporations]. An election is made on a timely-filed entity tax return.

Not all of these entities are able to make this election. Entities with partnership owners are disqualified, as are publicly traded partnerships and entities that can file combined tax returns.

The optional tax is elected on an annual basis by the entity, and once made cannot be revoked. Once the election is made, each partner/member/shareholder may elect to participate in the optional tax. The 9.3% tax is applied only to the distributive share of those who elect to participate.

This election is available for tax returns for the 2021-2025 tax years. It also sunsets if the federal SALT limitation is repealed. The 2021 tax is payable on the 2021 original due date of the California tax return (i.e., no extensions). For other years it is payable in two installments. The first is due June 15th of the tax year and is based on the prior year's elected tax. The second is due on the original due date of the entity's California tax return for the actual tax due less the amount of the first installment.

It should be noted that this tax is deductible by the entity on its federal return, but not on the California return.

Section 17052.10 grants participating owners of an electing entity a tax credit on their California tax return. That credit is 9.3% of their distributed share of income. If unused, this credit may be carried forward 5 years.

In enacting these laws, California keeps the same amount of tax receipts to which it originally was entitled while enabling entity owners a way to mitigate some of the SALT limitations imposed by the 2017 federal legislation. The benefits will vary depending on the circumstances of each owner, but they will surely outweigh the added complexity.

For further information, please contact your tax advisor or Alan Seher (aseher@nvlawllp.com).

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