

THE FEDERAL TAX REFORM PROPOSALS AND THE LIKELIHOOD OF A DISAPPEARING SALT DEDUCTION

Tax Alert
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Here's what you need to know about the likelihood of a disappearing SALT deduction.

We have hesitated to jump on the bandwagon of firms rushing to inform you of what you probably already know about the federal tax reform proposals from the mainstream media. But since the House and Senate have each now passed their own versions of tax reform, we thought you might like our take on what federal tax reform might mean for your year-end tax planning.

Of course, we have to start with a disclaimer: We don't know whether there will be federal tax reform in the near-term. But given the current appetite of Congress to address the issue, we assume that something will happen in the next few months. Then again, a lot could still happen in conference to de-rail this train.

We do know, however, that both Senate and House bills would remove the deduction for state and local income taxes and sales/use taxes (the "SALT deduction"), and in both cases, the removal of the SALT deduction would take effect in 2018. This is a huge issue for many taxpayers, and especially for those in high-tax states like New York, California, etc. And at this point, we think the proper approach is to assume rates will not go up and that the SALT deduction (for individuals) will be repealed.

What does that mean for individual (i.e. non-business) taxpayers?

2017 Estimates. If you don't expect to pay federal alternative minimum tax this year, you and your accountant should be thinking very hard about the state and local tax you'll pay on or before December 31. This could be the last year you can deduct SALT payments. Thus, even though the fourth quarter estimated tax payments for 2017 aren't due until January 15, 2018, don't wait! Pay those estimates before December 31. That's a no-brainer.

2018 Estimates? What about 2018 taxes? First quarter estimates for 2018 taxes, of course, are not due until April 2018. But if a taxpayer pays a reasonable estimate for 2018 taxes early, i.e., in December 2017, then the taxpayer should get the SALT deduction in 2017 since, as a cash-basis taxpayer, amounts were paid in calendar

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2017. This could be done manually by sending in a 2018 state estimated tax form and payment on or before December 31, 2017. Or better yet, in New York, if the taxpayer has an online tax account with the tax department, these estimates can be paid online. To illustrate, here's a screen shot from a payment screen:

So to pay 2018 estimates online, one could select "1st quarter 2018" from the drop-down box, enter the amount, choose a payment-posting date in 2017, pay the estimate and print the online confirmation! Or, taxpayers can mail in the paper form. Currently, as of December 11th, it does not appear that form is available on the tax department's website. But, here is a link to the form you could use.

Open State Tax Cases? What if you have an ongoing state tax audit or other disputed state tax liabilities? This is a stickier issue. If you make a down payment on a disputed tax issue with a state tax auditor before December 31, that should preserve your right to deduct it. But it might be tough to recoup a down payment if you end up in a settlement or negotiation posture later. So you should consult with your tax advisor (or us) to figure out how to best address this issue.

Finally, a few things to keep in mind. First, even if this federal tax reform package blows up, accelerating state tax payments in 2017 is generally a good strategy. This is because it appears very unlikely that top tax rates will be going up: No one is proposing that. So, at least for the foreseeable future, your SALT payments will be most valuable this year, in 2017, when federal tax rates are likely to be highest.

Also, and perhaps most importantly, beware of the Alternative Minimum Tax ("AMT") in 2017! You can pay all the state taxes you want in 2017, but if you are in the AMT you likely will lose the benefit of these extra SALT deductions. So it is critical that you and your accountant "run the numbers" to make sure you will be outside the AMT in 2017.

We understand that most people prefer to not pay taxes. And it's human nature to defer unpleasant actions to the last possible moment. But right now, it is particularly important to set aside any predispositions and sit down with your tax advisor to consider whether a proactive 2017 SALT payment approach might provide a worthwhile benefit.