Pass-Through Entity Tax Deduction

Background

- The TCJA limit on the deduction for state and local income taxes for individuals has a disproportionate impact on business owners who are operating as sole proprietorships, disregarded entities, or pass-through entities. The majority of America's businesses are structured as pass-through entities and are the backbone of our economy.
- Following the passage of TCJA, Treasury and the IRS approved the payment of a pass-through entity tax to be federally deductible in computing the entity's non-separately stated income or loss and is not taken into account in applying the federal cap to an individual partner or shareholder in the entity. 36 states have now passed legislation to mitigate the limitation on the federal income tax deduction for pass-through entities.
- Furthermore, TCJA significantly lowered the corporate tax rate and included several tax advantages for corporations that do not apply to pass-through entities.
- As Congress considers limits to businesses' ability to deduct various state and local taxes from their federal tax liability, Congress shouldn't give preference to one type of business structure over another.
- Based on informal feedback, the majority of pass-through entities have significant use of the pass-through entity tax deduction and feel that preserving the pass-through entity tax deduction is a high or the highest priority for them.
- Congress should retain the current ability for pass-through entities to fully deduct the entity's state and local income taxes on the business at the federal level.

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