



# OREA

OFFICE OF REVENUE & ECONOMIC ANALYSIS

# OREA EXPLAINS:

## The Pass-Through Business Alternative Income Tax

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### WHAT IS THE BENEFIT?

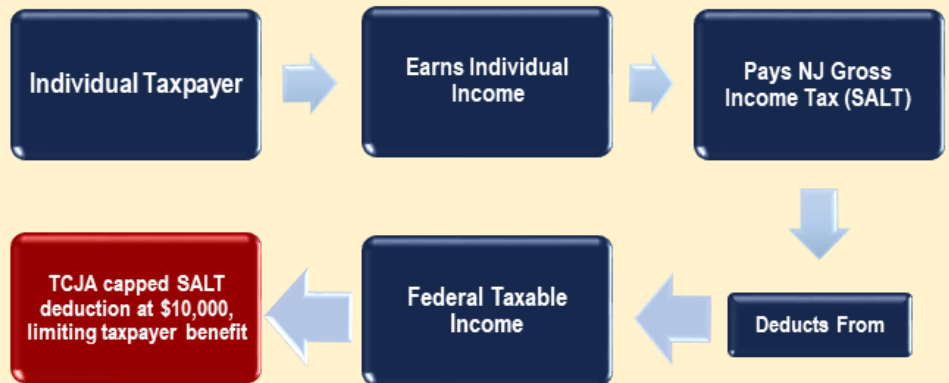
When the federal government capped the SALT deduction at \$10,000, limiting individual income taxpayer benefit, it did not place a cap on deducting business taxes paid to the State, so taxpayers can use PTBAIT to reduce their federal tax liability.

### What is the Pass-Through Business Alternative Income Tax?

The Pass-Through Business Alternative Income Tax (PTBAIT) is a tax option certain taxpayers can use to mitigate the effect of the State and Local Tax (SALT) deduction cap, created by the federal Tax Cuts and Jobs Act of 2017(TCJA). The PTBAIT allows members of partnerships, S corporations, and LLCs (pass-through entities) to pay their share of the business's taxable income as their taxable earnings rather than as personal income tax, allowing for greater deductibility. While PTBAIT provides benefits to certain taxpayers, it is expected to be revenue neutral for the State.

### How the Benefit Works for New Jerseyans

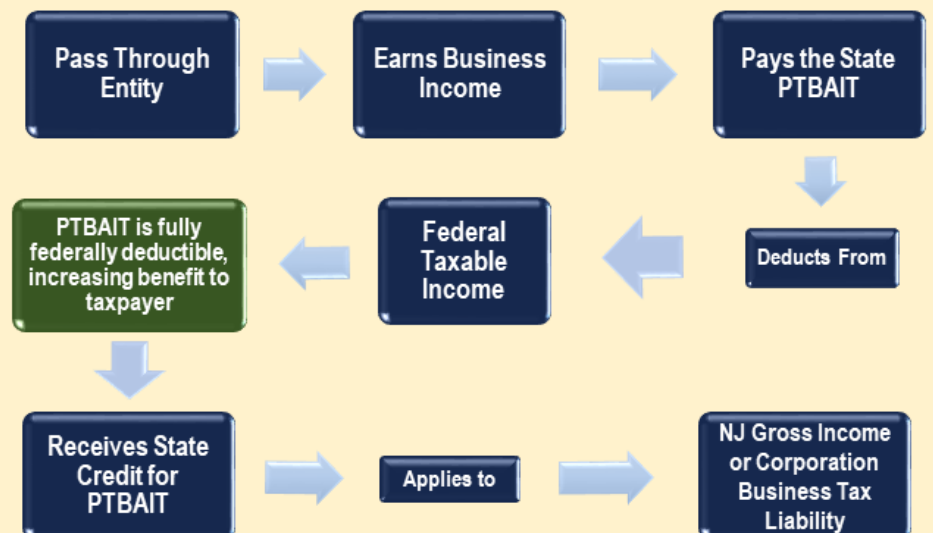
**The Issue:** Individuals were once allowed to deduct all of their SALT payments from their taxable federal income. The TCJA capped that amount at \$10,000.



### WHO CAN UTILIZE PTBAIT?

Business owners whose primary income comes from a partnership, S corporation, or LLC who previously took the SALT deductions from their federal income tax.

**The Solution:** Because TCJA did not cap the deductibility of business taxes, PTBAIT allows members of pass-through entities to continue deducting their state income taxes from their federal taxable income.



### NEW JERSEY AT THE FOREFRONT

New Jersey was one of the first states to enact this response to the SALT cap, along with WI, CT, LA, MD, OK, and RI. As of publication, 18 states have followed New Jersey's lead and enacted similar alternative tax structures.

**27,115**

The number of taxpayers that claimed PTBAIT credit on state tax filings through Nov. 2021.

## PTBAIT Tax Rates

Sum of Each Member's Share of Distributive Proceeds	Tax Rate
First \$250,000	5.675%
Amount over \$250,000 but not over \$1 million	6.52%
Amount over \$1 million but not over \$5 million	9.12%
Amount over \$5 million	10.9%

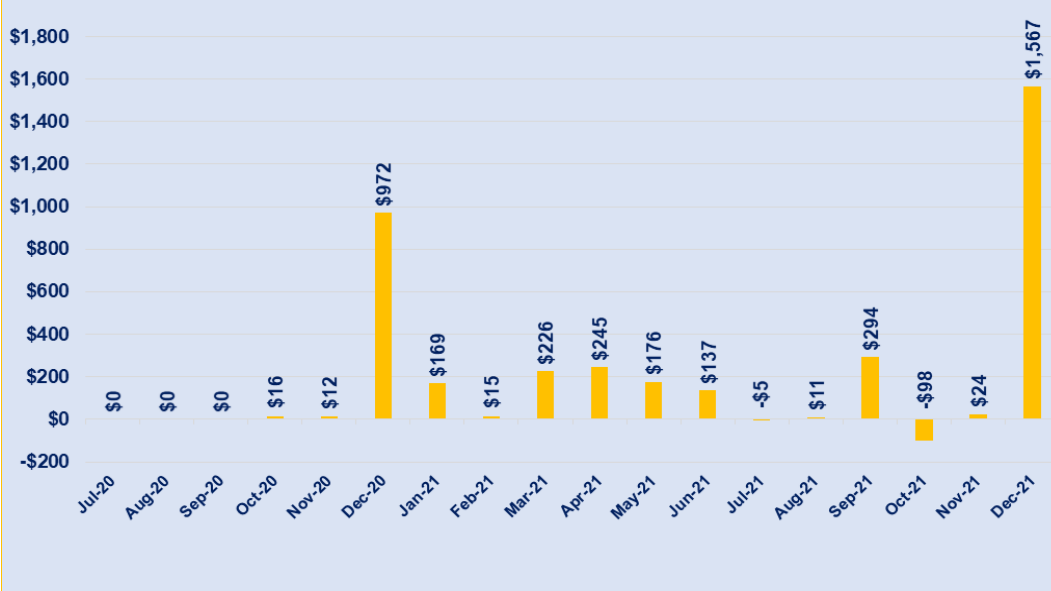
**OVER \$350 Million:** Estimated federal tax savings for New Jersey taxpayers utilizing the PTBAIT through Nov. 2021.

## PTBAIT & THE STATE BUDGET

The PTBAIT is expected to be revenue-neutral to the State over time. PTBAIT payments made during the tax year will be offset by credits applied when Gross Income Tax and Corporation Business Tax returns are filed.

The timing of payments created an initial revenue spike in FY 2021 when the federal approval for this tax structure wasn't settled until November of 2020. In December 2020 alone, the State received \$972 million in payments, half of which would have normally been estimated PTBAIT payments made in the first half of the tax year. Pass-through entities claimed \$1.2 billion in PTBAIT credit against New Jersey taxable personal or business income through November 2021.

**PTBAIT PAYMENTS**  
FY2021-22



It was expected that most of any annual increase in PTBAIT payments in tax year 2021 would be seen in quarterly estimated payments. However, December 2021 also saw a large surge in payments, with nearly \$1.6 billion collected.

This was largely because taxpayers who have not previously paid PTBAIT are not penalized for not making the estimated quarterly payments. As a result, many new PTBAIT taxpayers did not make payments until December, waiting to see if federal legislation affecting the SALT deduction was passed.

Taxpayers who had not made previous PTBAIT payments accounted for nearly \$700 million in December 2021.

## CONCLUSIONS:

- Recognizing that high-income states would be hardest hit by the Tax Cuts and Jobs Act of 2017, New Jersey implemented the Pass-Through Business Alternative Income Tax as a new option to help taxpayers reduce their federal tax burden.
- More than 28,000 pass-through entities have made either estimated or final PTBAIT payments as of January 4, 2022.
- The federal cap on SALT deductions is slated to expire in 2026. If the cap expires or is eliminated legislatively, the need for a PTBAIT also disappears.
- Additional information for tax planners can be found at: <https://www.state.nj.us/treasury/taxation/baitpte.shtml>



## SOURCES:

New Jersey Division of Taxation PTBAIT FAQ: <https://www.state.nj.us/treasury/taxation/baitpte-faq.shtml>  
 New Jersey Legislature, PL19, Ch. 320: [https://www.njleg.state.nj.us/Bills/2018/PL19/320\\_.HTM](https://www.njleg.state.nj.us/Bills/2018/PL19/320_.HTM)

## PTBAIT EXAMPLE:

The total New Jersey-sourced income of an LLC is \$1.5 Million, split evenly between LLC Member A and LLC Member B. The PTBAIT is imposed on the LLC's total income of \$1.5 million.

The LLC's tax is \$108,687.50.

$$(\$250,000 \times .05675) + (\$750,000 \times .0652) + (\$500,000 \times .0912) = \$108,687.50$$

Member A and Member B can each take a credit of \$54,343.75, or 50 percent of the total taxes paid by the LLC, against their state Gross Income Tax liability.

For their federal income tax filings, each Member can **deduct an additional \$54,344** from their taxable income for paying the PTBAIT, likely saving more than **\$16,000** in federal taxes each.