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New York judge dismisses blue state suit over SALT tax deductions

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- New York, along with New Jersey, Connecticut and Maryland, filed suit against Treasury Secretary Steven Mnuchin and the IRS back in July 2018.
- The states fought a new \$10,000 cap on the state and local tax deduction filers can claim on their federal income taxes.
- A federal judge in New York dismissed the states' suit on Monday.

On Monday, a federal judge dismissed a lawsuit filed by four states against the IRS, thwarting four blue states' challenge against a new \$10,000 cap on the deduction for state and local taxes, also known as SALT.

Those states — New York, New Jersey, Connecticut and Maryland — sued the Treasury Department, Treasury Secretary Steven Mnuchin and the IRS, among others, in [July 2018](#).

They alleged that the new limit on the SALT deduction, part of the Tax Cuts and Jobs Act of 2017, was “an unconstitutional assault on states' sovereign choices.”

In the dismissal, U.S. District Judge J. Paul Oetken in Manhattan said the plaintiff states ultimately failed to show that the SALT cap was unconstitutionally coercive or that it imposed on their own sovereign rights.

“[The] SALT cap simply requires the states to either exercise sovereign powers — howsoever they wish — to avert or assuage the cap's effects or else suffer the uncertain budgetary effects of doing nothing,” Oetken [wrote in his opinion](#).

Meanwhile, the states plan to fight back.

“There is no doubt in my mind that President Trump's unfair tax policy targets New York and other blue states by funding tax cuts for corporations and the rich on the backs of New Yorkers,” New York Gov. Andrew Cuomo, a Democrat, said in a statement.

“The bottom line is this policy is unprecedented, unlawful, punitive and politically motivated — and it must be stopped,” he said. “We disagree with the court's decision and are evaluating all options including appeal.”

In 2016, New Yorkers writing off state and local taxes took an average SALT deduction of \$21,779, according to the [Tax Policy Center](#).

Meanwhile, in New Jersey and Connecticut the average deductions were \$18,092 and \$19,563, respectively.

This development puts the ball back in Congress's court, said Michael D'Addio, principal at Marcum in New Haven, Connecticut.

"You know that the federal law is effective and it won't be overturned because this case has been dismissed," he said. "Unless you pressure your senators and representatives, there won't be a solution other than a congressional one."

Litigation against the federal government over the SALT deduction is following two tracks, according to Jared Walczak, director of state tax policy with the Center for State Tax Policy at the Tax Foundation.

One track — including the case that was just dismissed on Monday — argues that the SALT cap itself is unconstitutional.

The other track defends the different workarounds that the blue states have created to allow their residents to write off their state and local income and property taxes beyond the \$10,000 limit.

A second lawsuit filed in [July 2019](#) by New York, New Jersey and Connecticut in the Southern District of New York is still ongoing.

This time, the three states are suing to protect workarounds they built to permit taxpayers to claim deductions beyond the \$10,000 SALT cap.

The three states [passed legislation](#) that would permit municipalities to establish charitable funds to pay for local services and offer property tax credits to incentivize homeowners to give.

This way, the taxpayers could write off the payment as a charitable deduction on their federal tax returns.

In June, the IRS and Treasury [blocked this strategy](#), saying that the receipt of a state or local tax credit in return for making this contribution would be a "quid pro quo."

The new blue state "workaround" programs aren't the only ones that would be affected by the new IRS rules.

There are more than [100 existing state charitable tax-credit plans in 33 states](#), according to a research paper authored by a group of tax law professors. They range from private school tuition scholarships to conservation easements.

Earlier this year, some of those programs — including the Alabama Opportunity Scholarship Fund and the Exceptional SC program in South Carolina — [reported a slowdown in](#)

[contributions](#) due to ambiguity around whether the IRS would permit taxpayers to deduct the full amount donated.

Alabamans and South Carolinians contributing to those scholarship programs are eligible for a dollar-for-dollar tax credit on their state return.

Whether the final rule will ultimately deter people from donating to these funds remains to be seen.

“If you’re really passionate about private school vouchers in Georgia, you donate and you still get 100% of your donation back,” Carl Davis, research director at the Institute on Taxation and Economic Policy, told CNBC earlier. “You just won’t get a federal tax deduction on top of it.”