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Federal Tax Legislation Extends and Increases SALT Cap Preserves PTET Workarounds

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The One Big Beautiful Bill Act (OBBBA), signed into law by President Donald Trump on July 4, 2025, introduces a revised approach to the limitation on deductibility of state and local taxes (SALT cap).

Rather than making the current $10,000 SALT cap permanent as an earlier version of the OBBBA released by the Senate Finance Committee had proposed, the final bill offers temporary relief by raising the SALT cap to $40,000 for tax years 2025 through 2029. The expanded SALT cap applies to taxpayers with modified adjusted gross income (MAGI) of $500,000 or less and will be adjusted upward by 1% each year during that period.

For taxpayers with MAGI exceeding $500,000, the new SALT cap phases down by 30% of the amount over the threshold, though it never drops below the original $10,000 limit. After 2029, the SALT cap reverts permanently to $10,000 for all taxpayers, eliminating any ongoing benefit from the temporary expansion.

One of the most significant departures from an earlier House version of the OBBBA, which was discussed in this Cooley client alert, is the treatment of the pass-through entity tax (PTET) workaround to the SALT cap. As discussed in our prior alert, PTET elections generally permit entities, such as partnerships and S corporations (pass-through entities), to elect to pay state income taxes on behalf of their owners. These entities deduct the full amount of such taxes from their federal taxable income, and the owners receive a tax credit or other benefit from the state with respect to the taxes paid by the entity on the owners' behalf.

The result is that the state and local tax deduction – without any cap – is passed through to the owners as a reduction in their distributive share of the pass-through entity's net taxable income. In IRS Notice 2020-75, the US Department of the Treasury and IRS blessed the use of the PTET workaround by announcing an intent to issue proposed regulations confirming that PTET payments would be deductible pass-through entity expenses not subject to the SALT cap. Although no regulations have been proposed, many states have adopted legislation facilitating these PTET payments, and the structure is popular among pass-through entities and their owners.

While the House had previously proposed restricting PTET deductions for owners of service businesses – such as law firms, medical practices and investment advisers – the final bill did not adopt these limitations. Accordingly, pass-through businesses, including those in professional services, may continue to use PTET elections to bypass the individual SALT cap under current IRS guidance.

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