

**SALT Workaround Legislation: P.L. 2018, c. 11**

*[formerly S-1893 (Sarfo/Sweeney)/A-3499 (McKeon)]*

**Summary and Analysis - updated 5/4/2018**

S-1893/A-3499 passed the State Legislature in amended form on April 12 and was signed into law by Governor Murphy on May 4, 2018 (P.L. 2018, c. 11). The [text](#) of the final legislation is online at [http://njleg.state.nj.us/2018/Bills/S2000/1893\\_R1.PDF](http://njleg.state.nj.us/2018/Bills/S2000/1893_R1.PDF).

**Background**

The measure is intended to help mitigate the impact of the [new federal tax law](#) which caps federal deductibility of state and local taxes (SALT) to \$10,000, an amount lower than many New Jersey taxpayers have actually claimed in prior years. It would allow taxpayers to offset their property tax bills by “donating” to specific charitable funds that may be created by municipalities or school districts. The basic premise is that since the charitable giving tax deduction is not capped under the new tax law, taxpayers who itemize deductions on their federal returns would be able to circumvent the \$10,000 SALT limits.

**Charitable Funds and “Local Units”**

Under the legislation, a “local unit” (defined as a municipality, county or school district) would be permitted to, via ordinance or resolution, create one or more charitable funds “for specific public purposes of the local unit.” A fund’s “specific public purpose” must be “materially narrower” than the local unit’s general purpose, and funds must be maintained in a separate bank account.

The bill does not specify what an appropriate public purpose might be, although sponsors have given such examples as land conservation, food banks, college scholarships, support for public or private schools, support for poor or vulnerable populations, and construction of public roads.

Each fund must designate a “fund administrator” – a person or entity responsible for the collection and distribution of donated funds, and who must be “an official serving as the custodian of public funds for the local unit establishing the charitable fund.” Local units are not permitted to administer charitable funds jointly. The bill is silent about any of the other typical structural requirements for charitable organizations (NJ non-profit corporation status, federal 501(c)(3) recognition, boards of trustees and similar governance requirements, etc.).

The funds may use donations for one of the following purposes:

- (1) Payment of “any fees that may be required by a tax collector” to cover the tax collector’s administrative fees associated with compliance with the act.
- (2) The payment of administrative costs associated with the establishment of the fund; and
- (3) The remainder of the donations are to be used for purposes consistent with the specified charitable purpose of the fund.

**Annual Donation Cap**

An ordinance or resolution establishing a charitable fund must include an “annual donation cap” which limits the total amount of donations that can be made to a particular local charitable fund that may qualify for a tax credit. It also must create an annual limit on tax credit funding available as a result of

donations to the charitable fund; this limit is set at 90% of the annual donation cap unless the director of local government services establishes a different percentage. If a taxpayer makes a donation after the cap has been reached, the donation would be placed into a spillover fund to carry over into the next year. A taxpayer would be notified and given the option of redirecting the donation to another fund or rescinding the donation.

### **Property Tax Credits**

Anyone may donate to a charitable fund, but in order to receive credit against property tax liability, a property owner must direct the donation to the local fund where the property is based. If a taxpayer owns more than one property in a locality, s/he may designate a donation to be allocated across owned properties. Taxpayers would receive a 90% credit (or different amount as determined by the Director of Local Government Services of the NJ Department of Community Affairs) toward the tax liability for a specific property for each donation made to a local unit on behalf of that specific property. The credits are to be applied against the property owner's property tax bill. If the value of credits exceeds the amount of tax owed, the credits may be carried over for up to five years.

### **Amendments**

A series of [amendments](#) to the original legislation were adopted to protect property owners with mortgages, and to protect mortgage servicing entities, and to provide greater specificity regarding the fiscal accounting and use of the funds.

### **Implementation**

The NJ Department of Community Affairs' Division of Local Government Services and the NJ Department of Treasury are responsible for overseeing implementation. Regulations to be developed by these entities could include:

- Protecting local units against loss of property tax revenues due to operation of the property tax levy cap attributable to receipt of charitable donations;
- Establishing standard operating procedures for management of charitable funds
- Establishing appropriate timelines to coordinate the responsibilities of fund administrators and tax collectors
- Providing guidance to tax collectors and mortgagees
- Adjusting the annual donation percentage cap that may be credited against property tax payments

### **Comments and Questions**

While this bill is unquestionably a well-intentioned effort to lessen the negative effects of the new federal tax act, a number of issues arise with respect to its general framework as well as its particulars.

- 1) **Who benefits** – While the proposal could provide relief to some taxpayers, it remains available only to property owners who itemize on their federal returns, with many taxpayers left without access to its potential protections. Some have suggested that the bill would disproportionately benefit upper income taxpayers, while others counter that the high cost of living and property taxes in New Jersey would mean that its benefits would extend to many middle-class taxpayers as well. There is another argument that if this framework were to withstand legal challenge, it could push more taxpayers back to itemizing, which would make charitable deductions again available to them.
- 2) **Potential risk exposure for taxpayers** – Questions have been raised about whether this bill would pass muster legally, and whether taxpayers who make “donations” that are later overruled by the IRS could face a potentially significant federal tax liability as a result. U.S. Treasury Secretary Mnuchin has already spoken out strongly against the proposal, but putting

that aside, [some experts have noted](#) that if a taxpayer is getting a nearly 1:1 benefit for their gift, then a donation has not been made and a deduction therefore shouldn't be available. If this interpretation is accurate, then the best a taxpayer could hope for would be an interpretation that 10% of their payment (the amount in excess of the 90% cap) would be considered a donation. By contrast, U.S. Representative Josh Gottheimer (NJ-5) who first proposed the idea, has pointed to an [analysis published by the UCLA School of Law](#) to support claims of the validity of the framework.

The bill's sponsor has indicated that at least 100 programs have been adopted in 30 states that allow taxpayers to make charitable contributions to a variety of causes and providing tax credits for those who do. This statement is presumably based on the list provided in the appendix of the above-referenced [UCLA paper](#). More in-depth review is needed to determine the extent to which these programs mirror or differ from the framework presented in S-1893/A-3499, but it seems clear that many of the examples provided are significantly different.

- 3) **Complicated and potentially costly framework** – The framework as laid out in the bill seems extremely complicated. Depending on whether counties vs. municipalities choose to participate, it could result in the immediate creation of 566 new organizations (more, if school districts create separate funds) to carry out the purposes of the bill, each with its own fund administrator and administrative requirements/channels for taxpayer notifications, fund management, processing and the like. It is unclear whether the creation of funds within community foundations would be permissible for this purpose, but even if that is an option, the implementation requirements seem burdensome, confusing and potentially costly.
- 4) **Impact on charities and foundations** – Another question relates to what impact this framework could have on giving generally, which is already projected to drop significantly as a result of the new federal tax law. There is a concern that giving could be affected if taxpayers feel that they've already made their "donations" by paying their taxes via this mechanism, placing impossible pressures on foundations to fill the gaps and leaving vital needs unmet.
- 5) **What operational requirements will be established for the charitable funds?** The bill is silent about the need for charitable funds to meet specific legal, governance, and operational standards normally required of 501(c)(3) organizations. Examples include prohibitions against electioneering and private inurement, the requirement to establish a governing board and conflict of interest requirements, distribution of assets upon dissolution to another 501(c)(3) organization and others. Care must be taken to safeguard these local entities from potential malfeasance or misuse for personal or political gain.
- 6) **Conflating taxes and donations** – The bill raises a broader issue about the role of taxes and government generally and whether this proposal might further weaken the fundamental tenet that taxes are a necessary part of the functioning of government.

### Next Steps

While acknowledging that this bill will not solve all of the problems created by the new federal tax law, supporters view it as one way to try to soften the blow for New Jersey taxpayers. It's unclear when the IRS will issue a formal opinion or guidance as to the legality of the proposed framework. The Center for Non-Profits will continue to monitor this issue and will issue updated information as it becomes available. For more information, contact Linda Czipo at 732-227-0800 or email [lczipo@njnonprofits.org](mailto:lczipo@njnonprofits.org).