

SEC. 112018. LIMITATION ON INDIVIDUAL DEDUCTIONS FOR CERTAIN STATE AND LOCAL TAXES, ETC.

(a) IN GENERAL.—**Section 275** [deduction for certain taxes] is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

“(b) LIMITATION ON INDIVIDUAL DEDUCTIONS FOR CERTAIN STATE AND LOCAL TAXES, ETC.—

“(1) LIMITATION.—

“(A) IN GENERAL.—In the case of an individual, no deduction shall be allowed for—

“(i) any disallowed foreign real property taxes, and

“(ii) any specified taxes [see definition below] to the extent that such taxes for such taxable year in the aggregate exceed—

“(I) \$15,000, in the case of a married individual filing a separate return, and

“(II) \$30,000, in the case of any other taxpayer.

“(B) PHASEDOWN BASED ON MODIFIED ADJUSTED GROSS INCOME.—

“(i) IN GENERAL.—Except as provided in clause (ii), the \$15,000 amount in subparagraph (A)(ii)(I) and the \$30,000 amount in subparagraph (A)(ii)(II) shall each be reduced by 20 percent of the excess (if any) of the taxpayer’s modified adjusted gross income over—

“(I) \$200,000, in the case of a married individual filing a separate return, and

“(II) \$400,000, in the case of any other taxpayer.

“(ii) LIMITATION ON REDUCTION.—The reduction under clause (i) shall not result in—

The reduction under clause (i) shall not result in—

“(I) the dollar amount in effect under subparagraph (A)(ii)(I) being less than \$5,000, or

“(II) the dollar amount in effect under subparagraph (A)(ii)(II) being less than \$10,000.

“(C) MODIFIED ADJUSTED GROSS INCOME.—For purposes of this paragraph, the term ‘modified adjusted gross income’ means adjusted gross income increased by any amount excluded from gross income under section 911, 931, or 933 [certain non-US income].

“(2) **DISALLOWED FOREIGN REAL PROPERTY TAX.**—For purposes of this subsection, the term ‘disallowed foreign real property tax’ means any tax which— “(A) is a foreign real property tax’ means any tax which—

“(A) is a foreign real property tax described in section 164(a)(1) or 216(a)(1), and

“(B) is not an excepted tax.

“(3) **SPECIFIED TAX.**—For purposes of this subsection, the term ‘specified tax’ means—

“(A) any tax which—

“(i) is described in paragraph (1), (2), or (3) of section 164(a) [state and local, and foreign property taxes and income taxes], section 164(b)(5) [state sales taxes], or section 216(a)(1) [certain tenant-stockholder taxes], and

“(ii) is not an **excepted tax** [new defined term, see below] or a disallowed foreign real property tax, and

“(B) any **substitute payment** [new defined term, see below].

“(4) **EXCEPTED TAX.**—For purposes of this subsection—

“(A) **IN GENERAL.**—The term ‘excepted tax’ means—

“(i) any foreign tax described in section 164(a)(3) [foreign income tax],

“(ii) any tax described in section 164(a)(3) [state or foreign income tax] which is paid or accrued by a **qualifying entity** [new defined term, see below] with respect to carrying on a qualified trade or business (as defined in section 199A(d) [certain non-professional trade or businesses], without regard to section 199A(b)(3)) [income limits], and

“(iii) any tax described in paragraph (1) or (2) of section 164(a) [state property taxes], or section 216(a)(1) [certain state property taxes], which is paid or accrued in carrying on a trade or business or an activity described in section 212 [production of income including management of property].

“(B) **QUALIFYING ENTITY.**—For purposes of subparagraph (A), the term ‘qualifying entity’ means any partnership or S corporation with gross receipts for the taxable year (within the meaning of section 448(c)) if at least 75 percent of such gross receipts are derived in a qualified trade or business (as defined in section 199A(d), without regard to section 199A(b)(3)). For purposes of the preceding sentence, the gross receipts of all trades or businesses which are under common control (within the meaning of section 52(b) [controlled group of corporations])

with any trade or business of the partnership or S corporation shall be taken into account as gross receipts of the entity. “

“(5) **SUBSTITUTE PAYMENT**.—For purposes of this subsection—

“(A) **IN GENERAL**.—The term ‘substitute payment’ means any amount (other than a tax described in paragraph (3)(A)) paid, incurred, or accrued to any entity referred to in section 164(b)(2) [“**excepted tax**”] if, under the laws of one or more entities referred to in section 164(b)(2) [state, possession, or DC], one or more persons would (if the assumptions described in subparagraphs (B) and (C) applied) be entitled to **specified tax benefits** [new defined term, see below] the aggregate dollar value of which equals or exceeds 25 percent of such amount.

“(B) **ASSUMPTION REGARDING DOLLAR VALUE OF TAX BENEFITS**.—The assumption described in this subparagraph is that the dollar value of a **specified tax benefit** [new defined term, see below] is—

“(i) in the case of a credit or refund, the amount of such credit or refund,

“(ii) in the case of a deduction or exclusion, 15 percent of the amount of such deduction or exclusion, and

“(iii) in any other case, an amount determined in such manner as the Secretary may provide consistent with the principles of clauses (i) and (ii).

“(C) **ASSUMPTION REGARDING STATUS OF PARTNERS OR SHAREHOLDERS**.—The assumption described in this subparagraph is, in the case of any amount referred to in subparagraph (A) which is paid, incurred, or accrued by a partnership or S corporation, that all of the partners or shareholders of such partnership or S corporation, respectively, are individuals who are residents of the jurisdiction of the entity or entities providing the **specified tax benefits** (and possess such other characteristics as the laws of such entities may require for entitlement to such benefits).

“(D) **SPECIFIED TAX BENEFIT**.—For purposes of subparagraph (A), the term ‘specified tax benefit’ means any benefit which

“(i) is determined with respect to the amount referred to in subparagraph (A), and

“(ii) is allowed against, or determined by reference to, a tax described in paragraph (3)(A).

“(E) **EXCEPTION FOR NON-DEDUCTIBLE PAYMENTS**.—To the extent that a deduction for an amount described in subparagraph (A) is not allowed under this chapter (determined without regard to this subsection, section 170(b)(1), section 703(a), section 704(d), and section 1363(b)) [not clear how this reference is to be treated], the term ‘substitute payment’ shall not include such amount.

“(F) **EXCEPTION FOR CERTAIN WITHHOLDING TAXES**.—To the extent provided in regulations issued by the Secretary, the term ‘substitute payment’ shall

not include an amount withheld on behalf of another person if all of such amount is included in the gross income of such person (determined under this chapter).

“(6) REGULATIONS.—The Secretary shall issue such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this subsection, including regulations or other guidance—

“(A) to treat as a tax described in paragraph (3) of section 164(a) [income tax] any tax that is, in substance, based on general tax principles, described in such paragraph,

“(B) to treat as a substitute payment any amount that, in substance, substitutes for a **specified tax** [new defined term, see above],

“(C) to provide for the proper allocation, for purposes of paragraph (4)(A)(ii), of taxes described in section 164(a)(3) between trades or business described in section 199A(d)(1) and trades or business not so described, and

“(D) to otherwise prevent the avoidance of the purposes of this subsection.”

(b) **STATE AND LOCAL INCOME TAXES PAID BY PARTNERSHIPS AND S CORPORATIONS TAKEN INTO ACCOUNT SEPARATELY BY PARTNERS AND SHAREHOLDERS.—**

(1) IN GENERAL.—Section 702(a)(6) [items taken into account separately by partners] is amended to read as follows:

“(6)(A) taxes, described in section 901, paid or accrued to foreign countries,

“(B) taxes, described in section 901, paid or accrued to possessions of the United States,

“(C) **specified taxes** (within the meaning of section 275(b) [that is, the new subsection set out above]), other than taxes described in subparagraph (B), and

“(D) taxes described in section 275(b)(2) [that is, the new subsection set out above],”

(2) **TREATMENT OF SUBSTITUTE PAYMENTS** [new defined term—see above].—

Section 702) [items taken into account separately by partners] is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

“(d) TREATMENT OF **SUBSTITUTE PAYMENTS**.—Any substitute payment (as defined in section 275(b)(5) [the new section above]) shall be taken into account under subsection (a)(6)(C) [see above amended version—allocation between qualified and unqualified trade or businesses] and not under any other paragraph of subsection (a).”

(3) DISALLOWANCE OF DEDUCTION TO PARTNERSHIPS.—Section 703(a)(2)(B) [certain foreign taxes] is amended to read as follows:

“(B) any deduction under this chapter with respect to taxes or payments described in section 702(a)(6) [see above amended version],”. (4) S CORPORATIONS.—For corresponding provisions related to S corporations which apply by reason of the amendments made by paragraphs (1) through (3), see sections 1366(a)(1) and 1363(b)(2) of the Internal Revenue Code of 1986.”

(4) S CORPORATIONS.—For corresponding provisions related to S corporations which apply by reason of the amendments made by paragraphs (1) through (3), see sections 1366(a)(1) and 1363(b)(2) of the Internal Revenue Code of 1986.

(5) ALLOWABLE SALT DEDUCTIONS TAKEN INTO ACCOUNT FOR PURPOSES OF LIMITATION ON PARTNERSHIP LOSSES.—Section 704(d)(3) [limitations for allocations of losses] is amended by striking subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting before subparagraph (C) (as so redesignated) the following new subparagraphs:

“(A) IN GENERAL.—In determining the amount of any loss under paragraph (1), there shall be taken into account—

“(i) the partner’s distributive share of amounts described in paragraphs (4) and (6)(A) of section 702(a),

“(ii) if the taxpayer chooses to take to any extent the benefits of section 901, the partner’s distributive share of amounts described in section 702(a)(6)(B) [see above amended version], and

“(iii) the amount by which the deductions allowed under this chapter (determined without regard to this subsection) to the partner would decrease if the partner’s distributive share of amounts described in section 702(a)(6)(C) [see above amended version] were not taken into account.

“(B) TREATMENT OF POSSESSION TAXES IN EVENT PARTNER DOES NOT ELECT THE FOREIGN TAX CREDIT.—In the case of a taxpayer not described in subparagraph (A)(ii), subparagraph (A)(iii) shall be applied by substituting ‘subparagraphs (B) and (C) of section 702(a)(6)’ for ‘section 702(a)(6)(C)’.”

(6) CONFORMING AMENDMENT.—Section 56(b)(1)(A)(ii) [computing alternative minimum tax] is amended by inserting “or for any substitute payment (as defined in section 275(b)(5) [see above])” before the period at the end.

(c) **ADDITION TO TAX FOR STATE AND LOCAL TAX ALLOCATION MISMATCH.—**

(1) **IN GENERAL.**—Part I of subchapter A of chapter 68 is amended by adding at the end the following new section:

“SEC. 6659. STATE AND LOCAL TAX ALLOCATION MISMATCH [new defined term, see below].

“(a) **IN GENERAL.**—In the case of any covered individual, there shall be added to the tax imposed under section 1 for the taxable year an amount equal to the product of—

“(1) the highest rate of tax in effect under such section for such taxable year, multiplied by

“(2) the sum of the State and local tax allocation mismatches for such taxable year with respect to each partnership **specified tax** payment with respect to which such individual is a **covered individual** [new defined term, see below].

“(b) **COVERED INDIVIDUAL.**—For purposes of this section, the term ‘covered individual’ means, with respect to any partnership **specified tax payment** [new defined term, see below], any individual (or estate or trust) who—

“(1) is entitled (directly or indirectly) to one or more **specified tax benefits** [new defined term, see below] with respect to such payment, and

“(2) takes into account (directly or indirectly) any item of income, gain, deduction, loss, or credit of the partnership which made such payment.

“(c) **STATE AND LOCAL TAX ALLOCATION MISMATCH.**—For purposes of this section—

“(1) **IN GENERAL.**—The term ‘State and local tax allocation mismatch’ means, with respect to any partnership **specified tax** [new defined term, see above] payment, the excess (if any) of—

“(A) the aggregate dollar value of the specified tax benefits of the covered individual with respect to such payment, over

“(B) the amount of such payment taken into account by such individual under section 702(a) (without regard to sections 275(b) and 704(d)).

“(2) **TAXABLE YEAR OF INDIVIDUAL IN WHICH MISMATCH TAKEN INTO ACCOUNT.**—In the case of any partnership **specified tax** [new defined term, see above] payment paid, incurred, or accrued in any taxable year of the partnership, the State and local tax allocation mismatch determined under paragraph (1) with respect to such payment shall be taken into account under subsection (a) by the covered individual for the taxable year of such individual in which such individual takes into account the items referred to in subsection (b)(2) which are determined with respect to such partnership taxable year.

“(d) **DETERMINATION OF DOLLAR VALUE OF SPECIFIED TAX BENEFITS** [new defined term].—

“(1) IN GENERAL.—Except in the case of a covered individual who elects the application of paragraph (3) for any taxable year, the dollar value of any **specified tax benefit** [new defined term, see below] shall be the sum of—

“(A) the aggregate increase in tax liability (and reduction in credit or refund) for taxes described in section 275(b)(3)(A) [see above] for the taxable year and all prior taxable years that would result if such **specified tax benefit** were not taken into account with respect to such taxes, plus

“(B) the deemed value of any carryforward of such **specified tax benefit** (including any tax attribute derived from such benefit) to any subsequent taxable year.

“(2) DEEMED VALUE OF CARRYFORWARDS.— For purposes of paragraph (1), the deemed value of any carryforward is—

“(A) in the case of a credit or refund, the amount of such credit or refund,

“(B) in the case of a deduction or exclusion, the product of—

“(i) the highest rate of tax which may be imposed on individuals under the tax referred to in subsection (e)(3)(B) with respect to the **specified tax benefit**, multiplied by

“(ii) the amount of such deduction or exclusion, and

“(C) in any other case, an amount determined in such manner as the Secretary may provide consistent with the principles of subparagraphs (A) and (B).

“(3) ELECTION OF SIMPLIFIED METHOD.—In the case of a covered individual who elects the application of this paragraph for any taxable year, the dollar value of any **specified tax benefit** [new defined term, see below] shall be determined under the assumptions described in section 275(b)(5)(B).

“(e) OTHER DEFINITIONS AND SPECIAL RULES.— For purposes of this section—

“(1) PARTNERSHIP **SPECIFIED TAX PAYMENT**.—The term ‘partnership specified tax payment’ means any **specified tax** [new defined term, see above] paid, incurred, or accrued by a partnership.

“(2) **SPECIFIED TAX**.—The term ‘specified tax’ has the meaning given such term by section 275(b)(3) [new section above].

“(3) **SPECIFIED TAX BENEFIT**.—The term ‘specified tax benefit’ means any benefit which—

“(A) is determined with respect to a partnership specified tax payment, and

“(B) is allowed against, or determined by reference to, a tax described in section 275(b)(3)(A).

“(f) REGULATIONS.—The Secretary shall issue such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this section, including regulations or other guidance preventing avoidance of the addition to tax

prescribed by this section through partnership allocations that achieve similar tax reductions as a State and local tax allocation mismatch.”

(2) CLERICAL AMENDMENT.—The table of sections for part I of subchapter A of chapter 68 is amended by adding at the end the following new item:

“Sec. 6659. State and local tax allocation mismatch.”

(d) LIMITATION ON CAPITALIZATION OF **SPECIFIED TAXES** [that is, the taxes covered by the new subsection above].—Section 275, as amended by the preceding provisions of this section, is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

“(c) LIMITATIONS ON CAPITALIZATION OF **SPECIFIED TAXES**.—Notwithstanding any other provision of this chapter, in the case of an individual, **specified taxes** (as defined in subsection (b)) shall not be treated as chargeable to capital account.”

(e) REPORTING BY PARTNERSHIPS AND S CORPORATIONS WITH RESPECT TO SPECIFIED SERVICE TRADE OR BUSINESS INCOME.—

(1) PARTNERSHIPS.—Section 6031 is amended by adding at the end the following new subsection:

“(g) SPECIFIED SERVICE TRADE OR BUSINESS INCOME.—Returns required under subsection (a), and copies required to be furnished under subsection (b), shall include a statement of whether or not the partnership had any gross receipts (within the meaning of section 448(c)) from a trade or business described in subsection 199A(d)(2).”.

(2) S CORPORATIONS.—Section 6037 is amended by adding at the end the following new subsection:

“(d) SPECIFIED SERVICE TRADE OR BUSINESS INCOME.—Returns required under subsection (a), and copies required to be furnished under subsection (b), shall include a statement of whether or not the S corporation had any gross receipts (within the meaning of section 448(c)) from a trade or business described in subsection 199A(d)(2).”.

(f) CONFORMING AMENDMENT.—Section 164(b) is amended by striking paragraph (6).

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2025.