



TAX BULLETIN
RESTRICTED TAX CREDIT BULLETIN 2019-01

Claiming Donation-Based Tax Credits after the Tax Cuts and Jobs Act

Issued: January 3, 2019

The Department of Revenue provides this Restricted Tax Credit Bulletin to Pennsylvania taxpayers applying for and claiming donation-based state tax credits for tax years beginning after December 31, 2017 and before January 1, 2026. The purpose of this Restricted Tax Credit Bulletin is to explain the Department's treatment of contributions made to eligible organizations, in light of recent changes to federal tax law.

Background

On December 22, 2017, President Trump signed into law the legislation commonly known as the Tax Cuts and Jobs Act. On August 27, 2018, the United States Department of the Treasury proposed new regulations implementing certain provisions of the Tax Cuts and Jobs Act. 83 FR 43563 (Aug. 27, 2018).

The Department of the Treasury proposed amending the regulations promulgated under section 170 of the Internal Revenue Code (I.R.C.) to disallow a federal charitable deduction when a taxpayer receives state and local tax credits in exchange for contributions to certain entities listed in section 170(c) of the I.R.C. On September 5, 2018, the Internal Revenue Service issued a clarification stating that business taxpayers making "business-related payments to charities or government entities for which the taxpayers receive state or local tax credits can generally deduct the payments as business expenses," ¹

Prior to the enactment of the Tax Cuts and Jobs Act and the Department of the Treasury's proposed regulations, a taxpayer could receive a state tax credit for amounts contributed to an eligible organization and claim a federal charitable deduction for the same amounts. The Department of the Treasury's new regulations seek to end this practice.

Applicable Tax Credits after the Tax Cuts and Jobs Act This

bulletin applies to the following tax credit programs:

- Waterfront Development Tax Credit, 72 P.S. §§ 8701-K – 8710-K;

¹ See <https://www.irs.gov/newsroom/clarification-for-business-taxpayers-payments-under-state-or-local-tax-credit-programs-may-be-deductible-as-business-expenses>. (Last accessed Dec. 3, 2018).



- Neighborhood Assistance Tax Credit, 72 P.S. §§ 8901-A – 8907-A; and
- Any other tax credit where a state tax credit is awarded based upon donations.

The Waterfront Development Tax Credit Law states, “No tax credit shall be granted to a business firm for activities that are a part of its normal course of business or in which the business firm has a pecuniary interest.” 72 P.S. § 8708-K(2). Similarly, the Neighborhood Assistance Tax Credit Law states, “No tax credit shall be granted to any bank, bank and trust company, insurance company, trust company, national bank, savings association, mutual savings bank or building and loan association for activities that are a part of its normal course of business.” 72 P.S. § 8905-A. These sections do not prohibit a taxpayer from using a contribution as a business expense on the taxpayer’s federal return. The Department interprets these sections to mean that businesses are ineligible to receive state tax credits for payments made by a business firm in the normal course of a commercial transaction, such as providing a mortgage loan.

As long as the payment is not done in the normal course of a commercial transaction a taxpayer may claim the state credit for payments made to eligible organizations even if the taxpayer has claimed the payments as a deduction for federal income. For personal income tax only, a pass-through entity must make one adjustment to Pennsylvania taxable income as explained below.

Adjustment to Pennsylvania Income for Personal Income Tax

For personal income tax only, a “pass-through entity”, as defined by the specific tax credit law, must adjust its Pennsylvania income to account for contributions to an eligible organization for which it claims a deduction from its income on its federal tax return. This is consistent with how contributions were treated prior to the Tax Cuts and Jobs Act. Prior to the Tax Cuts and Jobs Act, the Department considered contributions to an eligible organization under the specific tax credit law to be charitable in nature. After the Tax Cuts and Jobs Act, the Department still considers contributions to be charitable in nature.

Therefore, a pass-through entity must add-back to its Pennsylvania income any amounts for which it received a tax credit and deducted as a business expense from its federal income. A pass-through entity cannot claim a deduction from its Pennsylvania income any amounts for which it received a Pennsylvania tax credit.

This bulletin is subject to change pending final approval of the federal regulations.