



TAX BULLETIN
RESTRICTED TAX CREDIT BULLETIN 2018-02

Claiming Educational Tax Credits after the Tax Cuts and Jobs Act

Issued: December 12, 2018

The Department of Revenue provides this Restricted Tax Credit Bulletin to Pennsylvania taxpayers applying for and claiming the Educational Improvement Tax Credit (EITC) and Opportunity Scholarship Tax Credit (OSTC) 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 pursuant to the Educational Improvement and Opportunity Scholarship Tax Credit Law, 24 P.S. §§ 20-2001-B – 20-2013-B ("Educational Tax Credit Law"), 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 or local tax credit for amounts contributed to a scholarship organization or educational improvement organization and claim a federal charitable deduction for the same amounts. The Department of the Treasury's new regulations seek to end this practice.

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).



Educational Tax Credit Law after the Tax Cuts and Jobs Act

Section 2006-B(b) of the Educational Tax Credit Law states, “No tax credit shall be approved for activities that are a part of a business firm's normal course of business.” This section does not prohibit a taxpayer from using a contribution to a scholarship organization or educational improvement organization as a business expense on the taxpayer’s federal return. In addition, the taxpayer may claim the state credit for payments made to scholarship organizations or educational improvement 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 in the Educational Tax Credit Law, must adjust its Pennsylvania income to account for contributions to a scholarship organization or educational improvement 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 a scholarship organization or educational improvement organization 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 an educational 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 tax credit under the Educational Tax Credit Law.

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

For additional information please visit The Department’s website www.revenue.pa.gov.