

Final regulations issued on charitable deductions related to state and local tax credits.

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Summary of Final Regulations: On June 11, 2019, the IRS announced that final regulations had been issued regarding the impact the receipt of state and local tax credits will have on charitable contributions. These final regulations also include the safe harbor provisions found in IRS [Notice 2019-12, which will provide a benefit to taxpayers in certain circumstances.](#)

The final regulations apply to contributions made after August 27, 2018, and generally retain the reduction to charitable contributions as set forth in the proposed regulations. The final regulations indicate that in general, taxpayers who make payments, or transfer property to an entity eligible to receive tax deductible contributions, must reduce their federal itemized charitable contribution deduction by the amount of any state or local tax credit the taxpayer received. The final regulations also adopted the *de minimis* exception allowing that no reduction to the charitable contribution amount will be required if the state or local tax credit received by the taxpayer is 15% or less of the taxpayer's contribution.

By incorporating the safe harbor provisions of Notice 2019-12 in the final regulations, a taxpayer will be allowed to treat the portion of a contribution that is disallowed due to the state and local tax credit, as an increase to the allowable state and local taxes included in itemized deductions. This increase would be includable with the other deductible state taxes shown on the Form 1040 Schedule A, but would be subjected to the \$10,000 (\$5,000 if married filing separately) limitation on the aggregate amount of state and local taxes.

Impact to North Dakota Charities: North Dakota state tax credit programs including the Nonprofit Private School Contributions Credit, the Planned Gift Tax Credit, and the Endowment Fund Contribution Credit all offer state tax credits that are more than 15% of the contribution amount. Therefore, under

the final regulations individual taxpayers will be required to reduce their federal itemized contribution amount by the value of any state and local tax credits received for making the contribution, subject to the safe harbor provisions described above. It is also worth noting that any portion of the qualifying tax credits, referred to above, used to determine federal taxable income will be an add back to ND taxable income.

Example: Assume a North Dakota taxpayer, filing jointly, makes a \$10,000 contribution qualifying for a 40% ND tax credit. This results in a \$4,000 reduction to the federal allowable charitable contribution, with the eligible amount of deductible federal charitable contributions reduced to \$6,000. Assuming the taxpayer is already itemizing \$4,000 in state and local taxes, adding the \$4,000 reduction in the allowable itemized charitable contribution amount, will result in total itemized state and local taxes of \$8,000. Since this total is still under the \$10,000 limitation, the full \$4,000 of disallowed contributions will be available to increase the state and local tax deduction for federal purposes. North Dakota taxable income must be increased by \$10,000, the combined amount of the charitable contribution and the state tax deduction reducing federal taxable income.

Assuming the same example above, but that the taxpayer was already deducting \$8,000 in state and local taxes, the \$4,000 reduction to the allowable itemized charitable contributions would result in state and local taxes of \$12,000. In this case, only \$2,000 of the disallowed contribution would be included with the deductible state and local taxes since the allowable state and local taxes are limited to the maximum \$10,000 deduction. In this case, North Dakota taxable income would be increased by \$8,000 (the \$6,000 charitable deduction and the \$2,000 of state income taxes deducted for federal purposes).

Next Steps: The IRS has said that they will be providing information in the future as to the reasons they made certain decisions in formulating the final regulations. And, while it may be cancelled due to the issuance of final regulations, in Notice 2019-12, there was a hearing scheduled to make comments on the safe harbor rules provided in the Notice. Anyone wanting to make comment on those safe harbor rules, written or electronic, should check

on the status of the hearing, and note that all comments must be received by the Treasury Department and the IRS by July 11, 2019. Submissions should be sent electronically via the Federal eRulemaking Portal at www.regulations.gov (use IRS - 2019-0020 in the search field to find the notice and submit comments) or can be mailed to:

CC:PA:LPD:PR (notice 2019-12)
Room 5203
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