



TaxNewsFlash

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Business taxpayer payments to state, local tax credit programs generally deductible; IRS response to inquiries on proposed regulations

The IRS today issued a release explaining that business taxpayers that make certain business-related payments to charities or government entities for which the taxpayers receive state or local tax credits generally can deduct the payments as business expenses.

Background

Proposed regulations released in late August 2018 include rules on the availability of charitable contribution deductions when the taxpayer receives or expects to receive in return a state or local tax credit. The proposed regulations generally require a taxpayer to reduce its charitable contribution deduction by the amount of a state or local tax credit received (or expected to be received) as a result of the contribution. This rule applies to individual and corporate taxpayers under section 170 and to trusts and estates under section 642(c). Read [TaxNewsFlash](#)

IRS response

Following the release of the proposed regulations, the IRS received inquiries as to what were the implications for business taxpayers making business-related payments to charities or government entities for which the taxpayer received state or local tax credits. According to today's IRS release—[IR-2018-178](#)—the general deductibility rule is unaffected by the proposed regulations concerning the availability of a charitable contribution deduction for contributions made to such programs.

The IRS release states:

The business expense deduction is available to any business taxpayer, regardless of whether it is doing business as a sole proprietor, partnership or corporation, as

long as the payment qualifies as an ordinary and necessary business expense. Therefore, businesses generally can still deduct business-related payments in full as a business expense on their federal income tax return.

The IRS also today added this information as a ["frequently asked question" \(FAQ\)](#) on state and local income tax, as follows:

Does the proposed regulation governing contributions in exchange for state and local tax credits affect the ability of a business that makes a payment under such a program to deduct the payment as an ordinary and necessary business expense?

No, the proposed regulation addresses the deductibility of such payments as charitable contributions under § 170. It does not affect the availability of a business expense deduction under § 162. A business taxpayer making a payment to a charitable or government entity described in § 170(c) is generally permitted to deduct the entire payment as an ordinary and necessary business expense under § 162 if the payment is made with a business purpose. The rules permitting an ordinary and necessary business expense deduction under § 162 apply to a taxpayer engaged in carrying on a trade or business regardless of the form of the business.

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