



DONATIONS

BUSINESS EXPENSE DEDUCTION AND STATE TAX CREDIT?

Recently released Federal Tax Regulations provide a potential dual benefit for individual owners of specified pass-through business entities (“PTEs”) who donate to scholarship granting organizations (“SGOs”).

Under the Final Regulations, a payment made by C corporations and PTEs to a charitable organization may qualify as an ordinary and necessary business expense deduction. By characterizing a charitable donation to an SGO as a business expense, C corporations and PTEs reduce their taxable income at the entity-level, and the individual owners of PTEs receive state and local tax (“SALT”) credits. The SALT credit generated by the business’s donation can be applied to the individual’s state tax liability, providing possible relief from the federal cap of \$10,000 on the SALT deduction.

WHEN DOES A CHARITABLE DONATION QUALIFY AS A BUSINESS EXPENSE?

If the payment is a reasonable, ordinary and necessary expenditure incurred in carrying on the trade or business, and the entity “reasonably believes the program will generate a significant degree of name recognition and goodwill in the communities where it operates and thereby increase its revenue,” then the donation may qualify as a business expense.

The Regulations provide an example stating a business may be entitled to a business expense deduction for payments made “for use in projects that improve conditions in the state.” Therefore, a donation to an SGO may be deductible as a business expense since the payment assist in providing greater educational opportunities, and greater educational opportunities improve educational outcomes. Improved educational outcomes in the state allow for fiscal and economic savings, and attract business to the state.

Tax benefit of contributing \$16,000 to Scholarships for Kids for Alabama income tax credit if contribution payment qualifies as business expense of pass-through entity owned by donor:

2023 FEDERAL INCOME TAX

	NO CREDIT	WITH CREDIT
WAGES	90,000	90,000
SCHEDULE E - S CORP	327,000	311,000 ⁽¹⁾
ADJUSTED GROSS INCOME	417,000	401,000
20% QBI DEDUCTION	(65,400)	(62,200)
STATE INCOME TAXES PAID	(10,000)	(10,000)
REAL ESTATE TAXES	(3,000)	(3,000)
MORTGAGE INTEREST	(12,500)	(12,500)
CHARITABLE CONTRIBUTIONS	(2,500)	(2,500)
ITEMIZED DEDUCTIONS	(28,000)	(28,000)
PERSONAL EXEMPTIONS	-	-
TAXABLE INCOME	323,600	310,800
INCOME TAX	65,335	62,263 ⁽²⁾
TAX CREDIT - DONATION TO SFK	-	-
INCOME TAX WITHHELD	25,000	25,000
ESTIMATED PAYMENTS	15,000	15,000
INCOME TAXES PAID 2023	40,000	40,000
TAXES OWED (REFUNDED) 2023	25,335	22,263

2023 ALABAMA INCOME TAX

	NO CREDIT	WITH CREDIT
WAGES	90,000	90,000
SCHEDULE E - S CORP	327,000	327,000 ⁽³⁾
ADJUSTED GROSS INCOME	417,000	417,000
FEDERAL TAX DEDUCTION	(65,335)	(62,263)
FICA/MEDICARE TAX DEDUCTION	(6,885)	(6,885)
REAL ESTATE TAXES	(3,000)	(3,000)
MORTGAGE INTEREST	(12,500)	(12,500)
CHARITABLE CONTRIBUTIONS	(2,500)	(2,500)
ITEMIZED DEDUCTIONS	(24,885)	(24,885)
PERSONAL EXEMPTIONS	(3,000)	(3,000)
TAXABLE INCOME	323,780	326,852
INCOME TAX	16,109	16,262.60 ⁽²⁾
TAX CREDIT - DONATION TO SFK	-	16,000
INCOME TAX WITHHELD	-	-
ESTIMATED PAYMENTS	-	-
INCOME TAXES PAID 2021	-	16,000
TAXES OWED (REFUNDED) 2022	16,109	262.60

WITHOUT DONATION: Federal Taxes: \$65,335 / State Taxes: \$16,109 = Total Expenses Paid: \$81,444

WITH DONATION: Federal Taxes: \$62,263 / State Taxes: \$262.60⁽³⁾ / Scholarships for Kids Donation: \$16,000 = Total Expenses Paid: \$78,525.60

Conclusion: \$2,918.40 Total Savings

1) Reduced by donation of \$16,000 to Scholarships for Kids as an ordinary business expense 2) Using Filing Status of Married Filing Joint 3) Assuming the \$16,000 donation deducted as a business expense by the S Corp for federal tax purposes must be added back for state income tax purposes in order to receive the tax credit against the Alabama income tax liability

The projections above are for illustrative purposes only, not intended as tax advice applicable to an actual situation. Please consult your tax advisor.



SCHOLARSHIPS for KIDS

REDIRECT 100% OF YOUR ALABAMA TAX LIABILITY UP TO \$100,000!

Because of the cap on Alabama tax credits (\$40 million in 2023), tax credits must be reserved through the Alabama Department of Revenue's ("ADOR") online reservation system.

HOW IT WORKS:



RESERVE

Go to myalabamataxes.alabama.gov, sign into or set up your MAT (My Alabama Taxes) account, report a donation to an SGO and choose SCHOLARSHIPS FOR KIDS.



DONATE

You have 30 days to remit your payment to Scholarships for Kids.



RECEIVE

The donation will be verified with the state. A receipt will then be generated to your "Correspondence" folder in your MAT account. You will also be mailed a receipt from Scholarships for Kids for federal income tax purposes.

For a list of our partner schools, or for more information, visit

SCHOLARSHIPSFORKIDS.ORG

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