

Corporate charitable contribution limitation

The following outlines the rules about limits which may apply to charitable contributions made by your corporation.

While corporations are entitled to tax deductions for charitable donations they make, the maximum deduction for any tax year is 10% of the corporation's taxable income. For this purpose, however, taxable income must be specially computed without regard to the following:

- (1) the charitable deduction itself, of course (which has not yet been determined).
- (2) the special corporate deduction for dividends received (generally 70% of the dividends received).
- (3) any net operating loss (NOL) carried back to the year from a future tax year.
- (4) any capital loss carried back to the year from a future tax year.
- (5) any deduction of premium on a repurchase of convertible debt.

Note that in 3 and 4, above, only if the NOL or capital loss is being carried back into the year from a future tax year is it disregarded. An NOL or capital loss that is carried forward into the year from an earlier year is used in determining taxable income for purposes of the charitable donation limitation.

Example (1): In Year 1, XYZ Corp. has \$200,000 in earnings from its operations, \$20,000 of capital gain, and \$10,000 in dividend income from corporations in which its interest is below 20%. It has \$40,000 in tax deductions not counting a charitable deduction or the dividends received deduction. It donated \$25,000 to qualifying charities in Year 1. In Year 2, XYZ has a \$5,000 capital loss which is carried back into Year 1.

The Year 1 charitable deduction is limited to \$19,000: 10% of taxable income of \$190,000 as determined solely for these purposes. The \$190,000 figure is arrived at by adding the earnings (\$200,000), the capital gain without reduction for the Year 2 capital loss carryback (\$20,000), and the dividend income without regard to the dividend received deduction (\$10,000). This total of \$230,000 is then reduced by deductions other than the charitable deduction (\$40,000) to obtain \$190,000.

XYZ's "real" taxable income can then be computed as follows: \$200,000 earnings, plus \$15,000 capital gains after the loss carryback, plus \$10,000 in dividends, but minus a \$7,000 (70%) dividends received deduction, the \$19,000 charitable deduction, and the \$40,000 remaining deductions. This comes to \$159,000.

Charitable contribution carryovers. Any charitable donations which cannot be deducted due to the limitation discussed above are carried forward into the following year where they can be deducted on top of the corporation's deduction for contributions made in that following year, subject to the same limitation as it applies in that year. If it can still not be deducted in the following year, it continues to be carried forward. However, if it is not used within five years after the year of the donation, it expires. Note as well that charitable donations in excess of the limitation amount can never be carried back to an earlier year, only forward.

If a contribution of property (as opposed to cash) is made by the corporation, the same rules that apply to non-corporate taxpayer contributions apply to determine the amount of the donation. These rules are applied first and then the total amount donated during the year is subject to the 10% limitation.