



YELLOWSTONE

Boys and Girls Ranch Foundation

THE “METC,” “SALT” and THE INDIVIDUAL MONTANA TAXPAYER

This paper is for the purpose of commenting on the recent SALT limitation Treasury Reg. §1.170A-1(h)(3)(i)) as it relates to the METC. It is not intended to serve as a commentary on the broader SALT law.

First, the definition of a couple of terms and a quick summary of “the problem...”

The “METC” (Montana Endowment Tax Credit) was passed into local law in 1997. The law was designed to promote Endowment growth for Montana charities. The statutes permitted a Montana income tax *CREDIT* for 40% of the allowable federal deduction (up to \$10,000 per taxpayer) for a “planned gift” that establishes a permanent, future endowment for a Montana based charity. Planned Gifts are defined in MCA §15-30-2327.

The “SALT” (State and Local Tax) limitation was enacted into law under the 2017 Tax Cuts and Jobs Act (TCJA). **SALT** limits the amount a taxpayer can deduct for *state and local taxes* to \$10,000 for joint filers (\$5,000 for single filers) on their federal income tax return.

The “PROBLEM” evolved after the **TCJA** was passed when several states created new “charities” to whom state taxpayers could make contributions and receive generous state tax CREDITS for their gift. These newly created “charities” would benefit only state and local government. *And since the SALT limitations do not apply to charitable contributions*, the contributions made to these newly created “charities” for local tax CREDITS would also generate charitable contribution deductions on the federal return.

Such a strategy would enable the taxpayer to “work around” the **SALT** limitation with the combined benefit of the state tax CREDIT and the federal deduction

possibly even exceeding the amount of money given away! IRS argued this strategy was a “quid pro quo” (rather than a “substance over form” argument).

The final regulation comments stated:

“If the Treasury Department and IRS were to allow taxpayers to claim a full charitable deduction for contributions made in exchanges for state tax credits, this treatment would result in significant federal tax revenue losses that would undermine the limitation on the deduction for State and Local Taxes in section 164(b)(6).”

So, the IRS proposed and made final Treasury Reg. § 1.170A-1(h)(3)(i) that would address this clever “work around.” However, in the process, IRS included existing state tax credit programs (such as the **METC**) even though on May 23, 2018 the Treasury Notice 2018-54 initially said that the proposed Regulation would NOT be applied to existing tax credit programs! Yet, when the Regulation was written, existing, “legitimate” state tax credit programs such as the beloved **METC** were not exempted.

The PRACTICAL So what does this mean to the Montana taxpayer who wants to capture the **METC** while putting in place a generous future endowment at their favorite charity? Is the **METC** still a valuable tax incentive for the Montana taxpayer and for charity’s endowment growth?

- **For the Itemizer on the Federal return-** The Regulation states that the taxpayer must reduce the Federal charitable deduction by the amount of the **METC** benefit received on the Montana tax return.

For example, if the individual Montana taxpayer establishes a “planned gift” (as defined in MCA § 15-30-2327) that qualifies for a **METC** in the amount of \$10,000, the taxpayer must reduce his charitable deduction on the federal tax return by \$10,000.

While reducing the overall federal tax savings benefit as a result of the **METC** planned gift transaction, this **SALT** regulation “*deduction haircut*”, does not eliminate the extra **METC** incentive for most Montana taxpayers. Those in federal tax brackets of 37% to 22% can still experience from over

40% to 80% greater tax savings from their gift by utilizing the **METC** as compared to simply taking a Montana charitable deduction.

- **For the Non-itemizer on the Federal return-** The Montana taxpayer who takes the Standard deduction on the Federal return (this may include 95% of all taxpayers due to the expanded standard deduction of \$12,000 single and \$24,000 joint filers) but itemizes on the Montana return will not experience any federal reductions as a result of the **METC** benefit.

For example, assume the individual Montana taxpayer establishes a “planned gift” generating a **METC** in the amount of \$5,000 but claims the standard deduction on the Federal return. The taxpayer will save the full \$5,000 from the **METC** CREDIT with no corresponding SALT Regulation “deduction haircut” since he is not itemizing on the Federal return.

The “Applicability” Date Since the “proposed regulations” were published August 27, 2018 and the final regulations were not released until June 11, 2019, the question as to when the Regulations apply is important. *The final Regulations apply to contributions made after August 27, 2018 (yes that is 2018)!*

This naturally begs the question, “What about those who claimed a Montana Endowment Tax CREDIT for gifts made in 2018 and who have already filed their tax returns for 2018?”

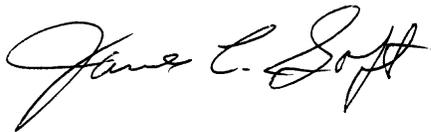
It depends! For those who take the standard deduction on the Federal return and itemized their deductions on the Montana return, no changes (i.e. no amended returns) are necessary.

For those who Itemize on both the federal and state returns, one of two scenarios are most likely.

First, if your return was prepared by an accounting firm, the likelihood is very high that amended returns will be unnecessary since most software programs had the **SALT** regulation already built in to the software system for 2018 tax returns (in anticipation that the proposed regulations would become final with minimal changes).

Second, if you prepared your own returns, you should check to see if the program you used included the final **SALT** regulations or, assuming you did your return by longhand, whether or not you reduced your Federal charitable deductions by the amount of **METC** claimed.

To read Treasury/IRS' full commentary/rationale on the final SALT Regulation, go to <https://federalregister.gov/d/2019-12418>.

A handwritten signature in black ink that reads "James C. Soft". The signature is written in a cursive, flowing style.

JAMES C. SOFT, President Emeritus
Yellowstone Boys and Girls Ranch Foundation