

Legal Fact Sheet

Pennsylvania Food Donation: Tax Incentives

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Federal tax incentives provide important financial incentives that make food donation more cost-effective and economically beneficial. These tax incentives have been extraordinarily successful in motivating food donation. In the past, federal tax incentives for food donations were limited to C-corporations.¹ Tax incentives for donations were temporarily expanded to cover more businesses in 2005. Following a series of temporary extensions, Congress subsequently made the expansion permanent in 2015,² providing all businesses with added incentive to increase food donations and prevent food waste. At the federal level, tax incentives are available in the form of general or enhanced deductions, each of which are discussed in this fact sheet.

Pennsylvania has adopted most of the current Internal Revenue Code for the calculation of business income and deductions.³ The provisions that cover the federal food donation tax deductions are included within those adopted by Pennsylvania.⁴ Further, a number of states have enacted state-level tax incentives. The Commonwealth of Pennsylvania provides a state-level tax credit to eligible businesses that donate food to approved organizations and programs through the Charitable Food Program.⁵ As such, businesses in the Commonwealth of Pennsylvania may claim the general or enhanced federal tax deductions for food donations. Additionally, businesses in Pennsylvania that donate food to an approved organization through the Charitable Food Program and are approved as contributors may receive a state tax credit

Federal Tax Incentives

How are the tax incentives calculated?

General (non-enhanced) tax deduction: Businesses that donate inventory may claim a tax deduction in the amount of the property's basis,⁶ which is usually the value of the property's cost to the business, and is often lower than the fair market value (the value at which goods can be sold). Businesses other than C-corporations—including S-corporations,⁷ sole proprietorships,⁸ and some LLCs⁹—cannot deduct more than either 30% or 50% of the business' total taxable income each year, depending on the type of organization to which the business is donating.¹⁰ C-corporations generally cannot deduct more than 10% of their taxable income each year.¹¹

Enhanced tax deduction: The enhanced tax deduction provides an extra incentive for donation by allowing the donating business to deduct the lesser of (a) twice the basis value of the donated food or (b) the basis value of the donated food plus one-half of the food's expected profit margin (if the food were to be sold at fair market value).¹² Under the enhanced deduction, all businesses may deduct up to 15% of their taxable income for food donations.¹³

Example: A grocery store donates potatoes with a fair market value of \$100. The basis value of these potatoes was \$30. The expected profit margin is the fair market value minus the basis value (\$100 - \$30), which is \$70. Under the enhanced deduction, the grocery store is eligible to deduct the smaller of:

$$(a) \text{ Basis Value} \times 2 = \$30 \times 2 = \$60, \text{ or } (b) \text{ Basis Value} + (\text{expected profit margin} / 2) = \$30 + (\$70 / 2) = \$65$$

The enhanced deduction would be \$60, which is substantially higher than the general deduction (the \$30 basis value).

Businesses that do not account for inventories and are not required to capitalize indirect costs will have the option to calculate the basis value at 25% of the products' fair market value.¹⁴ Businesses also have the option to calculate the fair market value of products that cannot be sold because of failure to meet internal standards, lack of a market, or similar reasons by using the price of the same or substantially similar, saleable food items.¹⁵

How can a donating business know if they are eligible for a tax deduction?

General tax deduction requirements: In order for a charitable contribution to qualify for a federal tax deduction, the donation must be used for charitable purposes and given to a qualified organization as laid out under section 170 of the Internal Revenue Code (IRC).¹⁶

Enhanced tax deduction requirements: In order to qualify for the enhanced tax deduction, a business must donate to a recipient organization that meets several criteria. First, the recipient must be a qualified 501(c)(3) not-for-profit as defined by the IRC.¹⁷ Additionally, the donor and recipient must meet the following requirements:¹⁸

(A) The recipient must use the donated food in a manner consistent with the purpose constituting that organization's exempt status under IRC 501(c)(3), which means that the donated food must be used exclusively for charitable purposes;

(B) The food must be used for the care of the ill, needy, or infants;

(C) The food may not be transferred by the recipient organization in exchange for money, other property, or services; however, the recipient organization may charge another organization a nominal amount for "administrative, warehousing, or other similar costs."

Example: If a business donates food to a food bank (the recipient organization), the food bank may not charge a soup kitchen for the donated food, and the soup kitchen may not charge the individuals eating at the soup kitchen. The food bank can, however, charge the soup kitchen a nominal fee for reimbursement of the costs of storing the food in a warehouse;

(D) The donating business must receive a written statement from the recipient organization. The statement must describe the contributed property and represent that the property will be used in compliance with the requirements outlined above; and

(E) The donated property must satisfy the requirements of the Federal Food, Drug, and Cosmetic Act (FDCA) at the time of donation and for the preceding 180 days. For food that did not exist for 180 days prior to donation, this requirement is satisfied if the food was in compliance with the FDCA for the period of its existence and at donation, and any similar property held by the donor during the 180 days prior to donation was also held in compliance with the FDCA.

All but three states with corporate income tax, including Pennsylvania, conform to the Internal Revenue Code calculation of corporate income tax in lines 1 through 28 of IRS Form 1120.¹⁹ In Pennsylvania and other states with I.R.C. conformity, businesses may be eligible to also count the federal food donation tax deduction in the calculation of their state income taxes. Businesses claim the charitable contribution deduction on Line 19 of IRS Form 1120.²⁰ The income amount used for the calculation of state taxes is already reduced by the amount of federal deductions, including charitable contributions, when it is transferred from Line 28 or Line 30 of IRS Form 1120 to state corporate income tax return forms.²¹

Pennsylvania Tax Credit

Over ten states currently offer state level tax incentives specifically for food donations.²² Pennsylvania is among those states and awards state level tax credits to certain eligible businesses that comply with a detailed application process. However, Pennsylvania is somewhat distinct from other states because the complexity of the program creates significant barriers to participation. The Pennsylvania Department of Community and Economic Development (DCED) administers the tax incentive through the Charitable Food Program within the Neighborhood Assistance Program (NAP).²³ The Charitable Food Program offers a 55 percent tax credit²⁴ to businesses²⁵ that donate money or food to qualifying charitable food organizations or projects approved under the program.²⁶

DCED manages the Charitable Food Program and is authorized to approve a wide range of food recovery organizations and projects in Pennsylvania, including "innovative food resource projects,"²⁷ such as gleaning projects, for participation in the program.²⁸ Importantly, only donations of food with "nutritional value," as determined by DCED, qualify for tax credits. Although DCED does not explain the criteria it uses to determine which foods have nutritional value, "candy, soda, [and] snack foods" do not qualify for the tax credit.²⁹

While Charitable Food Program is an important tax credit, the application process makes it difficult for many potential food donors to access the credit. Program projects and organizations are only approved for one year at a time.³⁰ To participate, charitable food recovery organizations and projects [“applicants”] must apply to DCED annually for approval. Applications must include a projected budget for the project and either: a) a solicitation plan for securing donations or b) letters from businesses [“contributors”] committing to donate a certain amount of food or money to the program applicant.³¹ If an applicant submits a solicitation plan lieu of letters, applicants must secure a firm commitment and Tax Compliance Form from each contributor and submit this information by September 30 of the year of the project.³²

Once applicants receive approval, the Pennsylvania Department of Revenue must then approve each contributor before the project starts. Each contributor must be tax compliant in order to receive approval.³³ If DCED accepts the application, the applicant secures contributors, and the Department of Revenue approves the contributors, the contribution period for the project takes place between July 1 of the project year and June 30 of the next.³⁴

After completing actual donations to the project, the approved contributors must submit an “Application for Tax Credit” with proof by December 31 of the year the project ends (18 months after the start of the contribution period) detailing the food contributions made on the program’s In-Kind Food Donations form.³⁵ The Department of Revenue will award tax credits to each approved contributor for 55 percent of the value of the food actually donated.³⁶

- Food donations of qualifying foods are valued by weight at costs predetermined by DCED.³⁷ For example, vegetables are valued at \$1.05/lb., resulting in a tax credit value of \$0.58/lb. of donated vegetables.³⁸
- Costs associated with activities necessary to support the project (e.g. transportation) are also eligible for the tax credit and must be included with explanations in the charitable food recovery organization’s application.³⁹

Contributor businesses may not receive more than \$500,000 per year in tax credits, unless they contribute to the operation of at least four qualifying projects, in which case they can receive up to \$1,250,000 per year.⁴⁰ Contributors may retain and use awarded credits themselves; carry them forward for up to five years; sell or assign them to a third party; or pass them through to their shareholders, partners, or members.⁴¹

Funding for NAP is limited at \$36 million per year.⁴² This 2019 change increased from the \$18 million in previous years.⁴³ Historically, DCED has allocated the Charitable Food Program around a sixth of the total funding available for the NAP,⁴⁴ if this holds true, DCED will allocate \$6 million to the program. Approval of tax credits for food donation is thus subject to availability, even for businesses that meet all program requirements.⁴⁵ This funding limit restricts the number of businesses that can benefit from Charitable Food Program.

Conclusion

In sum, businesses in the Commonwealth of Pennsylvania may claim the general or enhanced federal tax deductions for food donations. Because Pennsylvania has adopted the Internal Revenue Code provisions covering food donation deductions, eligible businesses also may claim the deductions when calculating their Pennsylvania state taxes. Furthermore, businesses in Pennsylvania that donate food to an approved organization or project through the Charitable Food Program and are approved as contributors may also be awarded a state tax credit.

¹ See I.R.C. § 170(e)(3)(C) (2017).

² See I.R.C. § 170(e)(3)(C) (2017); Protecting Americans Against Tax Hikes (PATH) Act of 2015, H.R. 2029, 114th Cong. § 113(a) (2015).

³ 72 PA. STAT. AND CONS. STATS. § 7401(3) (West 2018); 61 PA. CODE § 153.11 (2018).

⁴ 72 PA. STAT. AND CONS. STATS. § 7401(3) (West 2018); 61 PA. CODE § 153.11 (2018).

⁵ 72 PA. STAT. AND CONS. STATS. §§ 8901-a–8907-a (West 2019).

⁶ I.R.C. § 170(e)(1); Treas. Reg. § 1.170A-4(a)(1) (2018); Charitable Contributions: For Use in Preparing 2017 Tax Returns, I.R.S., DEP'T OF THE TREASURY 11, (Jan. 24, 2018), <http://www.irs.gov/pub/irs-pdf/p526.pdf> (noting the amount of the deduction is the fair market value minus the amount of income gained had the product been sold at fair market value).

⁷ I.R.C. § 170(b)(1)(B)(i); I.R.C. § 1363(b).

⁸ I.R.C. § 170(b)(1)(B)(i); Sole Proprietorships, I.R.S., <https://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Sole-Proprietorships> (last visited Oct. 29, 2018).

⁹ I.R.C. § 170(b)(1)(B)(i); Single Member Limited Liability Companies, I.R.S., <https://www.irs.gov/businesses/small-businesses-self-employed/single-member-limited-liability-companies> (last visited Oct. 29, 2018). Whether an LLC will be treated as an individual for tax purposes—and hence be subject to the 30% total charitable contribution cap—depends on the number of members in the LLC. *Id.*

¹⁰ I.R.C. § 170(b)(1)(A).

¹¹ I.R.C. § 170(b)(2)(A).

¹² See I.R.C. § 170(e)(3)(B); Treas. Reg. § 1.170A-4A(b)(4) (2017).

¹³ See I.R.C. § 170(e)(3)(C)(ii).

¹⁴ See I.R.C. § 170(e)(3)(C)(iv).

¹⁵ See I.R.C. § 170(e)(3)(C)(v).

¹⁶ See I.R.C. § 170(b)(c), (e)(3)(c).

¹⁷ See I.R.C. § 170(e)(3)(A).

¹⁸ I.R.C. § 170(e)(3)(A); Treas. Reg. § 1.170A-4A(b).

¹⁹ Federal Tax Reform and the States, NATIONAL CONFERENCE OF STATE LEGISLATURES (Apr. 1, 2018), <http://www.ncsl.org/research/fiscal-policy/federal-tax-reform-and-the-states.aspx>. Arkansas, Mississippi, and New Jersey do not conform to federal income tax calculations.

²⁰ See I.R.S. FORM 1120, U.S. CORPORATION INCOME TAX RETURN (2017).

²¹ See I.R.S. FORM 1120, U.S. CORPORATION INCOME TAX RETURN (2017).

²² These include Arizona, see Ariz. Rev. Stat. Ann. §§ 42-5074, 43-1025 (West 2016); California, see Cal. Rev. & Tax Code §§ 17053.12, 17053.88 (West 2016); Colorado, see Colo. Rev. Stat. Ann. § 39-22-301 (West 2016); Iowa, see Iowa Code §§ 190B.101–190B.106, 422.11E, 422.33(30) (West 2016); Maryland, see Md. Tax-Gen. Code Ann. § 10-745 (West 2018); Missouri, see Mo. Rev. Stat. § 135.647 (West 2016); New York, see N.Y. Tax § 210-B(52) (McKinney 2018); Oregon, see Or. Rev. Stat. §§ 315.154, 315.156 (West 2016); South Carolina, see S.C. Code Ann. § 12-6-3750 (West 2016); Virginia, see Va. Code Ann. § 58.1-439.12:12 (West 2016); and West Virginia, see W. Va. Code § 11-13DD-1:7 (West 2017).

²³ See 72 PA. CONS. STAT. §§ 8901-a–8907-a (2019).

²⁴ 72 PA. CONS. STAT. § 8905-A (2019).

²⁵ The law defines “[b]usiness firm” to mean “[a]ny business entity authorized to do business in [Pennsylvania] and subject to [its personal income tax, corporate net income tax, capitol stock-franchise tax, bank and trust company shares tax, title insurance company shares tax, insurance premium tax, or mutual thrift institutions tax].” See 72 PA. STAT. § 8902-A (West 2016).

²⁶ Eligible organizations include “[n]onprofit regional food banks, . . . and nonprofit emergency food providers that operate food pantries, soup kitchens, food banks, or other programs to relieve hunger, food insecurity, and food shortages among needy individuals and families, homeless people, and victims of domestic violence,” as well as “any programs that provides [sic] food to low income a [sic] target populations in a distressed areas [sic].” PA. DEP'T OF CMTY. AND ECON. DEV., NEIGHBORHOOD ASSISTANCE PROGRAM GUIDELINES 3 & 24 (2018), <https://dced.pa.gov/download/neighborhood-assistance-program-nap-guidelines/?wpdmdl=86209>.

²⁷ *Id.* at 23.

²⁸ *Id.* at 24.

²⁹ *Id.* at 25.

³⁰ *Id.* at 10.

³¹ *Id.* at 6-7.

³² *Id.* at 7 & 25.

³³ *Id.* at 10.

³⁴ *Id.* at 11.

³⁵ *Id.*

³⁶ *Id.* at 24 & Exhibit I.

³⁷ *Id.* at 26.

³⁸ *Id.* at Exhibit I.

³⁹ *Id.* at 25.

⁴⁰ *Id.* at 11.

⁴¹ *Id.* at 12.

⁴² 72 PA. CON. STAT. § 8905-A.

⁴³ 2018 Pa. Laws 2018-100 (H.B. 645) (West).

⁴⁴ PA. DEP'T OF CMTY. AND ECON. DEV., NEIGHBORHOOD ASSISTANCE PROJECT: HELPING BUILD SUCCESSFUL COMMUNITIES 3 (2018), <https://dced.pa.gov/download/neighborhood-assistance-program-impact/?wpdmdl=84815>. In 2017, only 10 CHARITABLE FOOD PROGRAM projects were approved; their contributors received a cumulative \$3,000,000 in tax credits. PA. DEP'T OF CMTY. AND ECON. DEV., 2017 NEIGHBORHOOD ASSISTANCE PROJECT AWARDS (Dec. 2017), <https://dced.pa.gov/download/statewide-nap-approvals-leg-districts/?wpdmdl=81018>. The same amount was allocated to 7 projects in 2016. PA. DEP'T OF CMTY. AND ECON. DEV., 2016 NEIGHBORHOOD ASSISTANCE PROJECT AWARDS (2016), <http://dced.pa.gov/download/nap-approved-2016-pdf/?wpdmdl=69471>. It is unclear whether this \$3 million award range will increase proportionately with the newly expanded funding.

⁴⁵ *Id.* at 7 & 11.