



RESTRICTED TAX CREDIT BULLETIN 2021-01

Limited Carryforward of Education Tax Credits

Issued: February 8, 2021

The Department of Revenue (“Department”) provides this Restricted Tax Credit Bulletin to explain the limited carry forward of credits permitted under Act 136 of 2020 and provide examples of the carry forward.

Act 136 of 2020

As a form of COVID-19 relief for taxpayers, Governor Wolf signed Act 136 of 2020 into law on November 25, 2020. Act 136 provides for a limited carry forward of unused educational tax credits, which includes the Educational Improvement Tax Credit (EITC) and Opportunity Scholarship Tax Credit (OSTC). For EITC and OSTC credits awarded during Fiscal Years 2020-2021 and 2021-2022, a business entity may carry forward unused credits or credits not passed through to the entity’s owners for two years. A business entity may include a C corporation or a pass-through entity such as an S corporation, partnership, limited liability company or special purpose entity. Only the business entity awarded the credits may carry the credits forward. The owners of a business entity that has been awarded credits may not carry forward any credits passed through to them. This includes special purpose entities’ owner/members.

Pass-through business entities not intending to carry-forward credits may elect to pass through the credits in whole or in part to their owners, but they must continue to pass the credits through to all the owners in proportion to the distributive income percentage of the owners. The limited carry forward of unused EITC or OSTC credits will not affect future applications for the credits. That is, when credits are carried forward, the amount of credits carried forward will not reduce the amount of credits which an applicant can apply for or use in a subsequent year.

Additionally, the REV-1123, Educational Improvement/ Opportunity Scholarship Tax Credit Election Form, will be revised to reflect the carryover provisions.

Examples

For each example below, a calendar year business entity (XYZ, LLC) is awarded \$25,000 in Educational Improvement Tax Credits in 2020. The entity has four partners (A, B, C, and D), each with an equal distributive income percentage of 25%.

Example 1

XYZ, LLC elects to pass the full \$25,000 credit to its owners. Each owner must receive \$6,250 of the total credit ($\$25,000 \times 25\%$). The owners must use the credit on their 2020 PA-40 tax returns, which will be filed during the 2021 calendar year.

Example 2

XYZ, LLC elects to pass \$4,000 of the \$25,000 credit to its owners. Again, the owners must receive a distribution of the credit in proportion to their distributive income percentage in XYZ, LLC. In this instance, each owner will receive \$1,000 of the credit ($\$4,000 \times 25\%$). The owners must use the credit on their 2020 PA-40 tax returns, which will be filed during the 2021 calendar year. The following chart shows the application of the credit by each owner.

Owner	Tax Liability	Distributive Income %	Credit	Liability after Application of Credit
A	\$2,000	25%	\$1,000	\$1,000
B	\$4,000	25%	\$1,000	\$3,000
C	\$1,000	25%	\$1,000	\$ 0
D	\$1,500	25%	\$1,000	\$ 500

XYZ, LLC will be permitted to carry the remaining \$21,000 credit forward for the next two succeeding tax years. XYZ, LLC will be able to pass the remaining credit to its owners in 2022 or 2023, or both years, depending on how much is passed through each year. When XYZ, LLC elects to pass the remaining credit to its owners, it must pass the credit in proportion to the owners' distributive income percentage.

Example 3

XYZ, LLC elects to pass \$15,000 of the \$25,000 credit to its owners. Again, the owners must receive a distribution of the credit in proportion to their ownership in XYZ, LLC. In this instance, each owner will receive \$3,750 of the credit ($\$15,000 \times 25\%$). The owners must use the credit on their 2020 PA-40 tax returns, which will be filed during the 2021 calendar year. The following chart shows the application of the credit by each owner.

Owner	Tax Liability	Distributive Income %	Credit	Liability after Application of Credit
A	\$2,000	25%	\$3,750	\$ 0
B	\$4,000	25%	\$3,750	\$ 750
C	\$1,000	25%	\$3,750	\$ 0
D	\$1,500	25%	\$3,750	\$ 0

Even though the amount of the credit passed through to Owners A, B, and D exceeds their 2020 tax liability, the owners are not entitled to a refund of the overpayment, nor are they allowed to carryforward the unused credit. XYZ, LLC will be permitted to carry the remaining \$10,000 credit forward for the next two succeeding tax years. XYZ, LLC will be able to pass the remaining credit to its owners for use on their 2022 or 2023 returns, or both years, depending on how much is passed through each year. When XYZ, LLC elects to pass the remaining credit to its owners, it must pass the credit in proportion to the owners' distributive income percentage.

Example 4

XYZ, LLC elects to pass none of the \$25,000 credit to its owners. In this instance, XYZ, LLC will be permitted to carry the entire \$25,000 credit forward for the next two succeeding tax years. XYZ, LLC will be able to pass the remaining credit to its owners in 2022 or 2023, or both years, depending on how much is passed through each year. When XYZ, LLC elects to pass the credit to its owners, it must pass the credit in proportion to the owners' distributive income percentage.