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Representing and Managing Tax-Exempt Organizations

Primer on Charitable Contributions

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I. Income Tax Deduction For Charitable Gifts

A. The percentage limitations for income tax deductions for charitable contributions by individuals.

1. Basic limit: 50% of taxpayer’s “contribution base” IRC § 170(b)(1)(A).

2. Contribution base = adjusted gross income computed without the net operating loss carryback deduction. § 170(b)(1)(F). Note only a carryback is excluded; a NOL carryforward will reduce the contribution base.

3. Note that the percentage is not a percentage of the gift.

4. Basic limit applies to all gifts; other limitations are simply sublimits within the basic limit.

a. however the only gifts that qualify for the full 50 percent limit are:

   (1) gifts of cash or property that is taken into account at its basis,

   (2) to (not “for the use of”):

   (3) public charities listed in § 170(b)(1)(A) or private foundations listed in § 170(b)(1)(E).

   (a) public charities listed in § 170(b)(1)(A) include: churches, hospitals, certain medical research organizations, educational organizations, organizations that support public colleges or

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universities, governmental units and organizations that normally receive a substantial portion of their support from a governmental unit or the general public.

(b) the private foundations listed in § 170(b)(1)(E) that qualify for the 50 percent limit are operating foundations, pass through foundations and pooled common funds.

b. all other gifts are subject to the special sublimit rules.

5. A contribution in excess of the 50 percent limitation may be carried over and deducted until exhausted for the five years following the year in which the gift is made. § 170(d).

a. Carryover deduction is subject to the same limit (50 percent of contribution base) for the year to which the carryover is made.

b. Result is to spread the deduction for a large gift (large in relation to the adjusted gross income of the donor) over up to six years.

c. In applying the limit for the carryover year, gifts to public charities made in that year are taken into account first.

(1) Although gifts of capital gain property are taken into account last, it appears that, for purposes of applying the carryover rule, a current gift of capital gain property to a public charity will be taken into account before a carryover gift of cash to a public charity. See Reg. § 1.170A-10(b)(2)(i).

d. If donor plans to make gifts of 30 percent capital gain property and 50 percent non-appreciated property, 50 percent property will count first. Consider making gift of undivided fractional interest in 50 percent property in order to spread it over two or more years.

6. Note that if the donor gives property that is not capital gain property or is tangible personal property that is not used by the charity in carrying out its exempt purpose, § 170(e) limits the deduction to the basis of the property.

a. In such a case the applicable limit is the 50 percent limit.

b. Donor can elect to have the 50 percent limit apply to gifts of capital gain property, if the donor does not take a deduction for the long term capital gain.
c. If property has a relatively high basis, consider making the election in order to use the 50 percent limit rather than the 30 percent limit. If the property has any gain at all, donor must make the election in order to use the 50 percent limit.

B. First 30 percent sublimit. § 170(b)(1)(B)

1. Applies to gifts “for the use of” any charitable organization or gifts to certain private foundations, i.e., a gift that does not qualify under § 1.170A-8(a)(2).

   a. A gift “for the use of” as opposed to a gift “to” a charitable organization is, in essence, a gift of an income interest in property whether or not the interest is in trust. Reg. § 1.170A-8(a)(2).

   (1) For example, a gift to a grantor lead trust is considered a gift “for the use of” the named charity because the charity’s interest is held in trust.

   (2) But a gift of a remainder interest in a charitable remainder trust is considered to be a gift of the remainder interest to the charity rather than a gift “for the use of” the charity unless the remainder interest will continue to be held in trust on termination of the charitable remainder trust. Reg. § 1.170A-8(a)(2).

   (3) Out of pocket expenses incurred in performing services for charity are considered a gift to rather than for the use of the charity; Rockefeller v. Comm. 767 T.C. 178 (1981), aff’d. 676 F.2nd 35 (2d Cir. 1982).

2. The 30 percent limit applies to all gifts to all private foundations other than operating foundations, pass through foundations, or pooled common funds.

   a. Note that gifts of “capital gain property” to private foundations (other than those listed in § 170(b)(1)(E)) are subject to a special 20 percent sublimit, discussed below.

   b. Capital gain property is any capital asset which, if sold at its fair market value, would generate a long term capital gain. § 170(b)(1)(C)(iv).

3. Limit is the lesser of:

   a. 30 percent of the contribution base or

   b. the excess of:
50 percent of the contribution base over; the amount of the contributions allowable under § 170(b)(1)(A); i.e. contributions to public charities or foundations listed in § 170(b)(1)(E) that qualify for the 50 percent limit determined without applying the second sublimit described below.

4. Thus, gifts of cash or property to a public charity in excess of 20 percent of the contribution base will reduce the sublimit for gifts to private foundations.

   a. For example, a taxpayer with a contribution base of $60,000 who makes a gift of $20,000 (33 percent of the contribution base) to a public charity will only have $10,000 (16.667%) of contribution base left to make a gift to a private foundation without running into a carryover situation.

   b. Note that in applying the limit, gifts of capital gain property to a public charity are not reduced by the 30 percent sublimit applicable to such gifts.

      (1) As a result, a gift of capital gain property to a public charity may reduce the sublimit for gifts to private foundations, even if the capital gain property is not fully deductible.

      (2) For example, suppose the taxpayer with a contribution base of $60,000 makes a gift of capital gain property worth $25,000 to a public charity and a cash gift of $20,000 to a private foundation.

         (a) the property gift is deductible only to the extent of $20,000 (30 percent of $60,000).

         (b) This would appear to leave $10,000 of the 50 percent limit available for the foundation gift.

         (c) But only $5,000 of the gift to the foundation is deductible, because the limit is 50 percent of the contribution base ($30,000 less the amount of the property gift, computed without the 30 percent limit, i.e. $25,000).

5. As in the case of contributions subject to the 50 percent limit, a contribution that exceeds the 30 percent limit may be carried forward to the five years following the year in which the gift is made and deducted in those years subject to the same limits in the carryover years; § 170(b)(1)(B).
a. For purposes of applying the carryover rules, all gifts made during the carryover year are taken into account before any carryover gifts.
b. Carryover gifts representing gifts to public charities are deemed to be gifts made during the year for purposes of applying carryovers of foundation gifts.

C. Second 30 percent sublimit: gifts of “capital gain” property. § 170(b)(1)(C).

1. “Capital gain” property is
   a. any capital asset which, if sold at its fair market value, would generate a gain that is taxable as long term gain and
   b. § 1231 property, i.e. property used in a trade or business which, by virtue of section 1221(2), is excluded from the definition of a capital asset. § 170(b)(1)(C)(iv).

2. Gifts of such property are deductible at fair market value without the recognition of gain and are therefore subjected to a lower limit than gifts of cash or property that is deductible at basis.

3. In applying the limits, gifts of capital gain property are taken into account after all other contributions (except for gifts of capital gain property to private foundations). § 170(b)(1)(C)(i).
   a. Thus, a cash gift to a public charity in excess of 20 percent of the contribution base will, in effect, reduce the 30 percent limit for gifts of capital gain property.
   b. For example, suppose a taxpayer with a contribution base of $60,000 makes a cash gift of $20,000. The maximum gift of capital gain property would be $10,000, the unused portion of the 50 percent limit; it would not be $20,000.

4. Special sub - sublimit for gifts of capital gain property to certain private foundations. § 170(b)(1)(D).
   a. Gifts of marketable securities to private non-operating foundations are deductible to extent of full fair market value. Donor may not give more than 10 percent of all outstanding stock of corporation.
   b. Gifts of capital gain property to private foundations other than marketable securities, such as real estate or closely held stock, are deductible only to the extent of basis.

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c. Gifts of marketable securities to private foundations (other than operating foundations, pass through foundations or pooled common funds) are subject to a special sub - sublimit in applying the second 30 percent sublimit.

d. Limit is lesser of:

   1. 20 percent of the contribution base or

   2. 30 percent of the contribution base less the gifts that qualify for the second 30 percent sublimit, i.e. gifts of capital gain property to public charities and § 170(b)(1)(E) foundations.

e. The special sub sublimit is applied after all of the other limits are applied. § 170(b)(1)(D).

5. Gift in excess of the limits are carried forward and deducted until exhausted in each of the five years following the year of the gift subject in each case to the same limit as applied in the carryover year and subject to the rule that gifts made during the carryover year are taken into account first. § 170(d)(1)(A)(i).

6. Under § 170(b)(1)(C)(iii), a taxpayer may elect to have capital gain property deducted at basis under § 170(e)(1) rather than at fair market value.

   a. If such an election is made, the 50 percent limit rather than the 30 percent limit applies, provided the gift is made to an (A) charity.

   b. Election applies to all gifts of capital gain property made during the year.

   c. Any carryover from an earlier year (in which the election was made) to a year in which such election is made must be recomputed as though the election had been made in the earlier year, but the taxpayer is not required to go back and recompute the deduction for the earlier year.

D. Gifts of S Stock

1. Outright Gifts Permitted

   a. § 1361(c), allows a donor to make an outright gift of S stock to charity. Previously a § 501(c)(3) organization could not be a qualified holder; therefore a gift of S stock, while deductible for income tax purposes subject to basic § 170 rules, caused loss of S
status. Under the current rule, if the gift is made to a charitable remainder trust or lead trust, the corporation loses S status.

b. Donor’s deduction is reduced under §170(e)(1) by the amount of any recapture or other ordinary income which would have been realized on sale of S corp assets as if the gift had been made in the form of a partnership interest.

c. All income paid out by S corporation to § 501(c)(3) shareholder is taxable as UBTI under § 512(e), including interest, dividends, rents, royalties and capital gain on sale of stock.

d. If § 501(c)(3) organization receiving gift of S stock is a trust rather than a corporation, capital gain generated in the S corporation including gain on sale of stock, is taxed at 20% trust capital gain rate rather than 34% maximum corporate rate.

e. If § 501(c)(3) trust pays out sale proceeds to another § 501(c)(3) entity, donor § 501(c)(3) trust obtains charitable deduction under § 512(b)(10), allowing deductions for such gifts up to 50% of adjusted gross income. This may reduce donor trust’s effective tax rate to 10% or less.

2. Tax Shelter Using S Stock

On April 26, 2004 the IRS issued Notice 2004-30 providing guidance on tax avoidance transactions involving S corporations and tax-exempt organizations structured to improperly shift tax away from the taxable S corporation shareholders to the exempt organization to avoid or defer tax. The transactions will be challenged on a number of grounds and are treated as “listed transactions” for purposes of tax shelter disclosure requirements. Promoters of listed transactions must keep list of investors and, in certain cases, register those transactions with the IRS. The transaction involves a S corporation which issues non-voting stock and warrants exercisable into non-voting stock on a pro rata basis to its original shareholders. The S corporation issues non-voting stock, for example, in a ratio of 9 to 1 voting/non-voting stock and warrants in a similar ratio. Thus, if the S corporation has a 1,000 shares of voting stock outstanding, the S corporation would issue 9,000 shares of non-voting stock and warrants exercisable into 9,000 shares of non-voting stock to the original shareholders exercisable over a period of years. The strike price on the warrants is equal to substantially all of the purported fair market value of the newly issued non-voting stock on the date granted and effectively reduces the fair market value of the non-voting stock because of the existence of the warrants. The original shareholders donate the non-voting stock to a charitable organization, taking an income tax deduction. Substantially all the taxable income is allocated to the non-voting stock and though such net income should be treated as unrelated under Section 512, either the exempt organization has net operating losses offsetting UBTI or has some other basis for claiming to be exempt from the UBTI. The shares are
typically redeemed for an amount equal to the fair market value of the stock as of the date the shares are presented for repurchase. The original shareholders, since they own all voting stock, can determine the timing and the amount of distributions. When the charity’s stock is redeemed or repurchased, it receives economic benefits from the stock ownership that are substantially less than the share of S corporation income allocated to it because the warrants effectively dilute the value of the shares held by the charity.

This transaction is similar to the Charity Family Limited Partnership (“CHAR-FLIP” or “CFLP”) previously promoted by certain tax shelters promoters.

E. Charitable Split Dollar Life Insurance, Annuity and Endowment Contracts

1. Charitable split-dollar arrangements, in which a donor makes a contribution to a charity that in turn funds a “personal benefit contract” (such as a split-dollar life insurance policy) that primarily benefits the donor’s family have been shut down. In Notice 99-36, the IRS announced its intent to deny a charitable deduction and impose tax evasion penalties on individuals and to penalize or revoke the tax-exempt status of charities that participate in such schemes.

2. §170(f)(10) denies the charitable deduction for split-dollar deals and impose an excise tax on participating charities. Exceptions are specifically created under §170(f)(10)(D) for gift annuity arrangements which a donee — charity chooses (or is required by law) to reinsure with a commercial insurer.

3. Form 8921 implements the reporting requirement for charities and other entities that acquire life insurance contracts that are structured to give both the exempt organization and private investors an interest in the contract.

F. Charitable Contributions Cars, Boats, and Planes and of Patents and Other Intellectual Property

1. Charitable Contributions of Cars, Boats and Planes

   a. IRC Section 170(f)(12) requires charities to provide a “contemporaneous” written acknowledgement that a donated vehicle, boat, or airplane will be used in direct furtherance of the donee’s charitable purposes or, with respect to a vehicle which is sold without material use or improvement, requires charities to advise the donor of the gross proceeds of the sale of the vehicle and that the amount of the donor’s deduction may not exceed the gross proceeds of the sale. The information contained in the acknowledgement must also be provided to the IRS. Knowing failure to provide the required acknowledgement can result in substantial penalties to the charity.
b. Existing law permits a donor of all tangible personal property including vehicles, boats and planes to claim a deduction based on the property’s fair market value (assuming that value exceeds the donor’s cost basis) only if the property is used by the charity for a use related to its exempt purposes; i.e. a painting given to a museum for its collection. Charities have for some time been required to report to the IRS the proceeds of disposition of certain donated property; however, the dollar threshold for filing such returns was generally $5,000. For vehicles, boats, and planes, the threshold is now only $500. Also, the charity must provide substantiation within 30 days after the date of the gift (for cars, boats, and planes used in direct furtherance of the donee’s purposes) or 30 days after the date of the sale (for property sold without material use or improvement).


a. Prior to the 2004 Act, the deduction generated by a gift of an intellectual property interest depended on the nature of the property transferred, with patents being treated more generously (a fair market value measure) and copyrights less generously (deduction limited to the lesser of fair market value or cost basis). For gifts of all intellectual property interests after June 3, 2004, the rule is now the same: the charitable income tax deduction is limited to the lesser of the donor’s adjusted cost basis in the property or the fair market value of the property.

b. Code Section 170(m) allows a donor an additional deduction for certain amounts in the year of contribution and in later tax years based on a sliding scale percentage of the so-called “qualified donee income” received by the charity that is allocable the donated intellectual property. This additional deduction is only allowed to the extent that the aggregate of the qualified donee income received or accrued exceeds the amount of the deduction claimed by the donor upon contribution of the patent or other intellectual property. Furthermore, the donor is required to give notice to the charity at the time of contribution that he intends treat the contribution as a qualified intellectual property gift and to claim the benefits of the additional deduction under Section 170(m). The deduction itself is limited to twelve years, with no income received or accrued after the tenth year (or, if sooner, the expiration of the legal life of the property) generating any further deduction base. This new deduction rule imposes burdens on charities which heretofore have not been required to compute separately the income received from distinct items of donated intellectual property. Questions also exist as to the effect of conditions imposed on a gift.
c. The charitable donee must file a Form 8899, Notice of Income From Donated Intellectual Property, with the IRS and provide a copy to the donor by the last day of the first full month following the close of donee's tax year.

G. Gifts of Fractional Interests in Tangible Personal Property.

1. Prior Law. Prior to the Pension Protection Act of 2006 ("PPA"), a charitable deduction was allowed for a gift of an undivided fractional portion of a donor’s entire interest in tangible personal property. This was an exception to the partial interest rule. Code Sections 170(f)(3)(B)(ii), 2055(e)(2) and 2522(c)(2). If it is reasonable to anticipate that the gift will be used in a manner related to the exempt purposes of the charity, and if the property would generate long-term capital gain upon its sale, the income tax deduction could be based on the relevant fraction of the entire fair market value of the property at the time of the contribution. Code Section 170(e)(1)(B)(i). If the charity’s use is unrelated, the deductible amount is limited to the relevant fraction of the donor’s basis in the property. No such distinction is made for purposes of computing the gift or estate tax charitable deduction.

2. Effective for gifts made after August 17, 2006, all interests must be owned either by the donor or the donee. No income tax deduction is available for a contribution of an undivided interest in tangible personal property unless immediately before the contribution all interests in the property were owned by the donor or by the donor and the donee charity. Code Section 170(o)(1)(A). In other words, there can be no other fractional interest owner (including for this purpose another charitable organization). The IRS is authorized to issue regulations that will permit separate donors who own undivided interests in the same item (for example, three siblings who inherited artwork as co-tenants) to make simultaneous proportionate contributions of such property to the same charity. Code Section 170(o)(1)(B). The limitation on owners applies for gift as well as income tax purposes. Code Section 2522(e)(1).

3. Deduction for additional gifts of undivided interests in the same property. If the use of the property is related to the charity’s exempt purpose, and the deduction is based on the fair market value of the property, there is a special limit on the amount of deduction generated by gifts to the same charitable donee of additional undivided interests in the same property. In that situation, the fair market value of an additional contribution is determined by using the lesser of (1) the property’s fair market value at the time of the initial fractional contribution or (2) the property’s fair market value at the time of the additional contribution. Code Section 170(o)(2). Therefore, no deduction is allowed for increases in the fair market value of the entire property after the time of the initial fractional
gift. (However, consistency is not an objective of the legislation since the
deduction is adjusted downwards if the property goes down in value after
the initial gift.) This rule initially also applied for purposes of calculating
the gift and estate tax charitable deduction for the transfer of a retained
interest, leading to a possible disjoint in the value of the property
transferred or includable in the estate and the amount of the permitted
charitable deduction. The Tax Technical Corrections Act of 2007 has,
however, amended both Code Sections 2055(a) and 2522(e) so that the
special limit no longer applies to the gift and the estate tax charitable
deduction.

4. Recapture of deduction and recapture penalty. If the prior change were
not a sufficient disincentive to make gifts of undivided interests in tangible
personal property, the Act also provides for the recapture of both the
income and gift tax (but not estate tax) charitable deductions in certain
circumstances. First, if the donor makes an initial contribution and then
fails to contribute all of the remaining interest in the property to the
original charitable donee (or if the donee is no longer in existence, to
another charitable organization) before the earlier of the 10th anniversary
of the initial gift and the donor’s death, there is recapture of the deductions
permitted for all prior contributions. (Question: Does “before the donor’s
death” mean that the gift must literally be completed before the donor dies
so that a bequest completing the gift will not satisfy the timing
requirement?) Secondly, there is also recapture where the charitable
donee fails to take substantial physical possession of the property, or fails
to use the property in a use substantially related to the organization’s
exempt function during the period beginning after the initial fractional
contribution and ending on the earlier of the 10th anniversary of the initial
contribution and the donor’s death. Code Sections 170(o)(3) and
2522(e)(3). The recapture takes the form of taxing the amount of the
recaptured deductions in the year in which the recapture is triggered, and
paying interest on any additional tax running from the due date of the tax
that would have been paid earlier if the deduction had not been claimed.
Furthermore, if a deduction is recaptured, there is an additional tax of 10%
of the amount recaptured. Code Section 170(o)(3)(B) and 2522(e)(3)(B).
There has been considerable ink spilled on this subject given that it has
effectively shut down fractional interest gift planning in this area. See
Stephanie Strom’s article in the New York Times, December 10, 2006,
entitled “The Man Museums Love To Hate,” focusing on Senator
Grassley, the former chairman of the Senate Finance Committee who was
largely responsible for initiating the PPA reforms.

5. Contributions before date of enactment. The Technical Explanation of the
Joint Committee on Taxation states that a contribution of an undivided
interest in tangible personal property before the date of enactment is not
treated as the initial fractional contribution for purposes of these rules.
The first additional undivided interest contribution after August 17, 2006
is instead treated as the initial contribution. Accordingly, the 10 year period runs from the date of the first contribution after August 17, 2006, not the date of the first prior contribution of an undivided interest in the same asset.

H. Recapture Rule for Certain Donations of Tangible Personal Property.

1. Prior Law. Under pre-PPA law, a charitable gift of tangible personal property that would generate long-term capital gain income if sold could be deducted for income tax purposes at fair market value provided that it was “reasonable to anticipate” that the charity would use the property for an educational, scientific or other charitable purpose (that is, a use related to the charity’s exempt purpose). Regulations interpreting this rule provided, for example, that if a donor contributed a work of art to an art museum, then, unless the donor had actual knowledge to the contrary, it would be reasonable for the donor to anticipate that the property would not be put to an unrelated use even if the museum later sold or exchanged the property. Charities disposing of donated property with a claimed value of more than $5,000 within two years after receiving the property were required to report the transaction to the IRS on Form 8282, with a copy being also provided to the donor.

2. Effective for gifts made after September 1, 2006, recapture of charitable deduction will be required absent a certification of exempt use if property is disposed of within 3 years. If the charitable donee disposes of “applicable property” within 3 years after the date of the contribution and the charity has not provided the donor with a “certification”, the donor’s deduction is subject to adjustment. If the disposition occurs in the same year as the gift, the adjustment is that the donor’s deduction is limited to basis. If the donated property is sold in a subsequent year but within 3 years after the contribution date, the donor must include as ordinary income for the year in which the disposition occurs an amount equal to the excess of (i) the amount of the charitable deduction previously claimed by the donor with respect to the property, over (ii) the donor’s basis in the property at the time of contribution. Code Section 170(e)(7).

3. Meaning of “applicable property”. This terms means appreciated tangible personal property that has been identified by the charitable donee as related use property and for which a deduction in excess of basis and in excess of $5,000 is claimed.

4. Meaning of “certification”. A certification is a written statement signed under penalty of perjury by an officer of the donee organization which either certifies that the property’s use was related to the donee’s exempt purpose or function and describes how the property was used and how such use furthered the donee’s exempt purpose, or states the intended use
of the property by the donee at the time of the contribution and certifies that such intended use became impossible or infeasible to implement.

5. Reporting requirements. The information return requirements that apply to the disposition of contributed property are extended to dispositions made within 3 years after receipt. Code Section 6050L(a)(1). In addition, the information to be reported must now include a description of the donee organization’s use of the property and a statement indicating whether such use was related to its exempt function. If the donee indicated a related use, it must also include with the return the certification discussed above.

6. Penalties. A $10,000 penalty is now imposed on anyone who identifies property as having a use related to the donee’s tax-exempt purpose or function knowing that the contributed property is not actually intended for that use. Code Section 6720B.

7. Practical Effect. Donations of tangible personal property for which a full fair market value deduction is claimed will be subject to increase scrutiny if the donee organization does not retain that property for at least three years after the date of the gift.

I. Charitable Contributions of Taxidermy

1. Prior Law. Accordingly, the charity must provide the donor with a contemporaneous written acknowledgement of the gift as described in Treasury Regulation Section 1.170A-13(f) in the same form as it would for any outright deductible contribution. In fact, the charity might want to go further and confirm that the contribution is not being added to a donor-advised fund or a supporting organization. Under pre-Act law, a charitable contribution of taxidermy property was subject to the regular tangible personal property rule. In the case of appreciated taxidermy, if the property was used to further the charitable donee’s exempt purpose, the deduction could be based on fair market value, but if the property was not used to further the donee’s exempt purpose, the deduction would be limited to basis. If instead the taxidermy property was worth less than the taxpayer’s basis in the property, the taxpayer could generally deduct the fair market value of the contribution, regardless of whether the property was used for related or unrelated purposes by the charitable donee. According to the Humane Society of the United States and articles in the Wall Street Journal, these rules were being exploited by trophy hunters. Such individuals were, for example, claiming the costs of exotic hunting excursions as part of their basis in donated taxidermy property, thereby writing off their travel and accommodation expenses through the guise of a charitable deduction.

2. Limitation on Deduction. After 2006, for taxidermy property contributed by an individual who prepared, stuffed, or mounted the property or by a
person who paid or incurred the cost of preparation, stuffing or mounting, the amount of the charitable contribution deduction is now required to be reduced by the amount of the gain that would have been long-term capital gain if the property had been sold by the taxpayer at its fair market value. Fair market value is determined at the time the contribution is made. Code Section 170 (e)(1)(B)(iv). Accordingly, the amount now allowable as a deduction for a charitable contribution for taxidermy property is the lesser of the donor's basis in the property or the fair market value of the property, regardless of the intended use by the donee organization.

3. Basis Determination. If taxidermy property is contributed and a charitable contribution deduction is claimed by the person who prepared, stuffed or mounted the property or by any person who paid or incurred the cost of such preparation, stuffing or mounting, only the cost of preparing, stuffing, or mounting the taxidermy property may be included in calculating the basis of the property. Code Section 170(f)(15)(A). The effect of this special rule is to limit basis to direct costs. Indirect costs, such as transportation, equipment or other costs related to hunting or killing the animal, are not included in the measure of basis and are, accordingly, not deductible.

4. Definition of “Taxidermy Property”. Taxidermy property means any work of art which (1) is the reproduction or preservation of an animal, in whole or in part, (2) is prepared, stuffed, or mounted for purposes of recreating one or more characteristics of such animal, and (3) contains a part of the body of the dead animal. Code Section 170(f)(15)(B). This is a much narrower definition than contained in earlier drafts of the legislation. Under those drafts, it was feared that taxidermy property could include works of mixed media composed partially of silk. Donations of Damien Hirst's formaldehyde suspended cows and sharks may not fare as well, however.

5. Effective Date. This provision applies for all contributions made after July 25, 2006.


1. IRA Rollover. For close to ten years the charitable world has promoted the enactment of the so-called “IRA rollover” as a way to allow donors with significant wealth in retirement plans to fund charitable gifts during lifetime without the recognition of taxable income. Without such legislation, a donor who withdraws IRA assets and then gives them away is required to include the IRA withdrawal in income and then may not be able to offset the income completely due to the adjusted gross income limitations on charitable deductions and other limits on itemized deductions. Furthermore, the recognition of income may cause loss of tax exemptions or increased taxes on social security benefits and other items.
For these reasons, tax advice has often focused on the use of retirement plan assets to fund charitable gifts at death. The new rollover provision expired on January 1, 2008, and was extended annually, most recently on December 15, 2014. The recent extension benefitted only donors who delayed minimum required distributions until the end of December, 2014. Congress may repeat the extension adoption again in 2015 for this year only, or possibly make this provision permanent. Key points to note about the IRA rollover include:

a. **Age 70½.** A donor (including apparently the beneficiaries of inherited IRAs) must have reached age 70 1/2 at the time of making the qualified charitable distribution (“QCD”) to take advantage of this provision.

b. **IRA Only.** A donor may exclude from income up to $100,000 of QCDs made from traditional or Roth IRA accounts, but not from other deferred compensation accounts. All IRAs are aggregated for purposes of this rule. For married individuals filing a joint tax return, the limit is $100,000 per individual IRA owner (and accordingly a maximum of $200,000 for the couple if both have separate accounts of sufficient size).

c. **Minimum Required Distribution.** The rollover to charity will count toward the minimum distribution requirements of traditional IRAs.

d. **Substantiation.** The charity must receive the payment directly from the IRA custodian or trustee and must provide the donor with contemporaneous written acknowledgement (the same as for an outright gift). Accordingly, the charity must provide the donor with a contemporaneous written acknowledgement of the gift as described in Treasury Regulation Section 1.170A-13(f) in the same form as it would for any outright deductible contribution. In fact, the charity might want to go further and confirm that the contribution is not being added to a donor-advised fund or a supporting organization. Recent IRS guidance indicates that a check drawn on an IRA account and delivered by the donor/IRA owner to the charity will be considered a direct payment by the IRA trustee/custodian for these purposes.

e. **Only Certain Public Charities Qualify.** A donor must give to a public charity such as a school, hospital, church or other publicly supported organization described by IRC Section 509(a)(1) or (2). Private foundations (other than conduit or operating foundations) are not eligible recipients. In addition, even though they otherwise qualify as public charities for income tax deduction purposes, distributions made to supporting organizations and donor-advised funds are not treated as QCDs for purposes of the legislation. It
comes as no surprise, therefore, that the IRS has issued guidance (in Announcement 2006-93) on how a supporting organization can request a change in public charity classification to publicly supported status.

f. No Quid Pro Quo. Although the rules do not permit the donor to claim a separate income tax charitable deduction for the distribution, the entire amount of the QCD must be otherwise allowable as a charitable income tax deduction under IRC Section 170 (ignoring the percentage limitation rules). As a consequence, a QCD cannot be used to fund a pooled income fund gift or a charitable remainder trust, nor can it be used to purchase a charitable gift annuity. Also, the donor cannot receive any quid pro quo benefit. If a benefit is received, the entire amount of the QCD will constitute taxable income.

g. May Satisfy Pledge. Notice 2007-7 states that a QCD may be used to satisfy a donor’s preexisting pledge without violating IRS prohibited transaction rules.

h. Roth IRAs. Most Roth IRA distributions are non-taxable. Accordingly, these provisions are of limited utility for owners of Roth IRAs.

i. Who Benefits?

(1) Non-itemizers. Non-itemizers now receive the equivalent of a deduction if they make gifts directly from their IRAs to qualified charities.

(2) “Maxed-out” Donors. At the other end of the spectrum are donors who have maximized their ability to claim income tax deductions on a current year basis due to the 50% contribution base limitation. Since QCDs operate independently of the percentage limitation rules, these donors can now give more and receive an income tax benefit.

(3) Greater income tax efficiency. While the old rules required donors to take the IRA distribution into income and then permitted a deduction, the result was not always a wash, particularly for high income taxpayers. Receiving additional income affected the taxation of social security, the application of the alternative minimum tax, the deductibility of medical expenses and miscellaneous deductions, the availability of certain credits and the overall impact of itemized deductions.
(4) State Taxes. If a donor’s state income tax law does not allow a charitable deduction but generally follows the federal definition of taxable income (for example, Massachusetts), making a gift from an IRA should now provide the equivalent of a state charitable income tax deduction. Each state law needs to be checked carefully before reaching such a conclusion.

2. Enhanced deduction for conservation contributions.

a. In brief, the 2006 rules were designed to encourage taxpayers to make contributions of capital gain property for “qualified conservation purposes”. The enhanced deduction rules have also been extended repeatedly from year to year, most recently in December, 2014 for 2013 and 2014. Under both pre-Act and post-Act law, these purposes include:

b. preservation of land areas for outdoor recreation by, or for the education of, the general public;

c. protection of natural habitats and other ecosystems;

d. preservation of open spaces for the scenic enjoyment by the general public or pursuant to a clearly delineated government conservation policy where such preservation will yield a significant public benefit; and

e. preservation of an historically important land area or certified historic structure.

f. The types of contributions embraced by the rules include gifts of the donor’s entire interest in the real property (other than a mineral interest), a remainder interest in real property, or a restriction granted in perpetuity on the use of the real property. Organizations to which such contributions can be made include government units, certain publicly supported charities, and supporting organizations of such charities. The charity must have a “commitment to protect the conservation purposes of the donation and have the resources to enforce the restrictions”. Treas. Reg. Section 1.170A-14(c)(1).

g. General provisions. For an individual donor, the annual deduction limit for qualified conservation contributions (“QCCs”) was increased to 50% of the donor’s contribution base, rather than the normal base of 30%. Code Section 170(b)(1)(E)(i). If the value of the donor’s contribution exceeds the 50% contribution base, the excess could be carried forward for 15 years. Code Section 170(b)(1)(E)(ii). The contribution base and carry forward rules for
donations of QCCs are applied separately from those that apply to other donations. Code Section 170(b)(1)(E)(iii). This is intended to preserve the full impact of the extended carry forward rule.

h. **Special rules for contributions of property used in agriculture or livestock production.** If the individual is a “qualified farmer or rancher” for the tax year in which the QCC is made and if the contribution includes a restriction that the property remain “generally available” for agriculture or livestock production, the individual’s contribution base is increased yet higher to 100%. Code Section 170(b)(1)(E)(iv)(I). Note that the latter “generally available” requirement is only applicable to contributions made after August 17, 2006, and that it is not necessary that the property actually be used in agriculture or livestock production; it must only remain available for such purposes. Thus, the land could be used for recreation or public education so long as it might be used for ranching. The 100% contribution base limitation applies first to contributions other than QCCs that meet its special requirements (to the extent allowable under other rules) and then to the agricultural QCCs. A 15 year carryforward is again permitted. To be a qualified farmer or rancher, the individual’s gross income from the trade or business of farming must be greater than 50% of the individual’s gross income for the tax year. Code Section 170(b)(1)(E)(v).

i. **Corporate farmers and ranchers are also eligible.** Enhanced deductibility rules also applied to corporate farmers and ranchers, provided that the corporation’s stock was not readily tradable on an established securities market at any time during the contribution year. Code Section 170(b)(2)(B).

K. **Planning with the income tax deduction limits**

1. Limits affect relatively few donors.

2. Planning opportunities fairly limited.

3. If gift exceeds the limits plus the carryover, consider deferring a portion of the gift to a later year in order to spread the gift over more than six years.

   a. technique will be frustrated if donor does not live for the carryover period.

   b. if value of property decreases, deferral could be self defeating.

4. If basis of property is high relative to value, and the 30 percent limit creates a problem, consider making the § 170(b)(1)(C)(iii) election to
deduct property at basis in order to obtain the benefit of the 50 percent limit. Time value of money may be critical here.

5. The carryover expires on the death of the donor.
   a. If the donor is married to a healthy spouse, consider converting the property to joint property and making a joint gift in order to decrease the risk that death will terminate the carryover.
   b. But if the gift is a joint gift, note that the death of spouse will terminate the carryover with respect to one half of the gift; the carryover amount attributable to the deceased spouse must be taken, if at all, on a separate return filed by the surviving spouse. Reg. § 1.170A-10(d)(4)(iii).

II. Income Tax Deduction - limits on gifts by corporations. § 170(b)(2).

A. Corporations are subject to a simple limit of ten percent of taxable income computed without regard to:
   1. The charitable contribution;
   2. The dividend received deductions and other special corporate deductions (other than the special deduction for organizational expenses provided by § 248);
   3. The net operating loss carryback deduction;
   4. Any capital loss carryback;
   5. The amount of any corporate gift in excess of the 10 percent limit may be carried forward and deducted until exhausted in the five years following the year of the gift, regardless of whether the gift is made to a public charity, or to a private foundation.

B. Type of asset (cash or property) is irrelevant as is the form of the contribution (to or for the use of) and the type of charity to which the contribution is made.

C. As with individuals, corporations are allowed a five year carryover for contributions that exceed the limit.

D. Capital gain property and § 1231 property are deductible at fair market value; all other property (e.g., inventory) is deductible at basis.

E. Special rules for contributions of inventory:
   1. § 170(e)(3). Contributions of property to charity that uses the property solely for the care of the ill, the needy, or infants;
2. § 170(e)(4). Tangible personal property:
   a. constructed by the taxpayer,
   b. contributed not more than two years after construction to:
   c. an institution of higher education or a scientific research organization,
   d. which uses the property for research, experimentation or research training, in the physical or biological sciences, in the United States.

3. §170(e)(6). Contributions of computer technology and equipment for elementary or secondary school purposes.
   a. contribution made within two years after constructed or acquired by taxpayer
   b. contributed to school or support organization
   c. substantially all use of the property is for educational purposes in grades K-12

4. in either case, property is deductible at fair market value less sum of:
   a. one half of the unrealized ordinary income;
   b. plus excess, if any, of deduction over 2 X basis.

5. for example, if fair market value is ten and basis is 2, deduction is 10 - (4+(6-(2 X 2))) or 4. Without the special rule, the deduction would have been 2.

6. Effect of the special rule is to give a deduction for the lesser of 2 X basis or basis plus one half of the ordinary income.

7. to qualify, charity cannot sell the property and must furnish the donor with a written statement that the property will be used in accordance with the statute.

F. Charitable Contributions of Food and Book Inventory Enhanced by the Katrina Emergency Tax Relief Act of 2005.

In 2005 various short-term incentives were adopted to increase charitable giving. Two such incentives, both dealing with inventory property, were extended by the PPA but expired on January 1, 2008. These provisions have been re-enacted from year to year, most recently in December, 2014 effective through 2014. They may be extended further in 2015.
(1) **Donations of “apparently wholesome food” inventory by non-corporate taxpayers engaged in a trade or business.** Such donations are entitled to an enhanced deduction equal to the lesser of (1) the donated item’s cost basis plus one-half of its appreciation and (2) twice the donated item’s cost basis. The amount for which a deduction may be claimed is limited to 10% of the taxpayer’s aggregate net income from the trade or business from which such contribution is made. Code Section 170(e)(3)(C).

(2) **Donations of book inventory by corporate taxpayers.** Corporations other than S corporations are entitled to an enhanced deduction for donations of book inventory to public schools that provide elementary or secondary education. The donee organization is required to certify in writing that the books are suitable for use in its educational programs and that it will actually use the books. Code Section 170(e)(4)(D).

G. A gift by an S corporation is not subject to the corporate limits; it is passed through to the shareholders on the K-1 and subjected to the individual limits on the shareholders’ return. § 1366(a)(1).

H. **PPA Changes to Basis of S Corp. Holdings.**

(1) **Prior Law.** Pre-PPA law provide that if an S corporation contributes money or other property to charity, each shareholder is permitted to take into account the shareholder’s pro rata share of the contribution in determining the shareholder’s own income tax liability. Code Section 1366(a)(1)(A). The shareholder’s basis in the S corporation stock is then reduced by the amount of the charitable contribution that flows through to the shareholder. Code Section 1367(a)(2)(B). This is generally the fair market value of the contributed property. Furthermore, the contribution may not reduce the shareholder’s basis below zero, effectively limiting an S corporation shareholder’s ability to deduct a charitable contribution made by the S corporation to the shareholder’s basis in the stock. Code Section 1366(d).

(2) The 2006 Act modified the basis reduction rules only for S corporation gifts. It provided that the amount of the shareholder’s basis reduction in the stock by reason of the corporate contribution equals the shareholder’s pro rata share of the **adjusted basis** in the property contributed, not the pro rata share of the contribution’s fair market value.
Code Section 1367(a)(2). This appeared to have the effect of permitting a fair market value deduction for the contributed property without causing shareholders to recognize gain or a reduced loss that is attributable to the appreciation on a subsequent sale of the stock. It also equated the treatment of S corporation gifts and partnership gifts with respect to basis adjustment. See Rev. Rul. 96-11, 1996-1 C.B. 140.

Revenue Ruling 2008-16 confirms the view expressed in the legislative history that the intent of the PPA provision was to permit an S corporation shareholder to deduct his or her pro rata share of the fair market value of the contributed property, as a partner in a partnership is permitted to do. While prior law, an S corporation shareholder’s charitable deduction was limited to his or her basis in the S corporation stock, this ruling provides a detailed calculation for determining the amount of the charitable deduction allowed in the case before it, which will serve as useful guidance for future situations if the legislation is extended. In addition to the revenue ruling, a technical correction enacted just days before the provision expired confirmed that a fair market value deduction was permitted. Code Section 1367(a)(2) as amended by P.L. 109-280, Section 1203(a). The favorable S corporation provision expired on January 1, 2008, but has been re-enacted from year to year, most recently in December, 2014 effective through 2014.

(3) Any amount disallowed will be carried forward indefinitely. § 1366(d)(2).

(4) Any deduction taken will reduce the shareholder’s basis in the S corporation stock. To the extent that the contribution exceeds the individual’s basis in the stock, it may be carried forward and deducted against any future increase in the basis of that stock. § 1367.

I. Alternative Minimum Tax - Deduction Limitations.

Under some circumstances a taxpayer who is subject to the alternative minimum tax would be in a better position vis-a-vis the 30% - 50% deduction limitations if he or she could use adjusted gross income as redetermined for alternative minimum taxable income purposes, taking into account the items of AMT adjustment provided in Sections 56 and 58 and the items of AMT preference provided in Section 57. Reg. Section 1.55-1 specifically provides that, for taxable years beginning after December 31, 1993, for purposes of calculating AMTI, all references to
adjusted gross income (including the limitation on charitable contribution deductions) should be based on AGI for regular (not AMT) income tax purposes. A letter from Robert M. Brown of KPMG Peat Marwick to the Commissioner of Internal Revenue dated May 17, 1994 commented on that regulation in proposed form and stated that the regulation was contrary to Congressional intent and contrary to two private letter rulings, 9320003 and 9321063. The letter strongly opposed the proposed regulation, advocating instead that a taxpayer should be able to choose whether to use the regular definition of adjusted gross income or to use the adjusted AMTI definition if more favorable.

III. Limitations - Trusts and Estates

A. The percentage and other limitations contained in § 170(b)(1) apply only to individuals and relate to the deduction taken under § 170(a).

B. § 642(c)(1) provides a trust or an estate a deduction “in lieu of” the deduction under § 170(a) for any amount of the gross income, without limitation which, pursuant to the terms of the governing instrument, is paid during the taxable year for a charitable purpose.

C. Thus, trusts and estates are allowed a charitable income tax deduction limited only by gross income; no need for carryover.

   1. A private foundation that has lost its exemption is not entitled to the benefits of § 642(c) and is instead subject to § 170 - see § 642(c)(6).

   2. If a trust has income which, if it were exempt, would be treated as unrelated trade or business income:

      a. Any deduction with respect to that income may not be taken under § 642(c)(1). See § 681(a).

      b. Deduction is not lost; such trusts are entitled to take deductions under § 170(a), subject to the limits as though they were individuals. Reg. § 1.681(a)-2(a).

      c. Limits are applied to the UBTI rather than the “contribution base.”

IV. Impact of Recent Legislation on Charitable Contributions

A. Changes in the top rate:

   1. Top ordinary income rate is now 39.6% and top capital gains rate (imposed also on qualified dividend income) is now at 20% on capital assets held more than 12 months. 28% and 25% capital gains rates apply to certain other assets.

a. Key Concepts and Mechanics

(1) Applicability

(a) Tax on NII is intended to apply to:

1) Individual taxpayers; and
2) Trusts and estates.

b. Tax Rate

(1) Tax is assessed at 3.8%.

1) The tax on NII is assessed in addition to regular income tax. Aggregate federal rates on interest, nonqualified dividends and short-term capital gains can be as high as 43.4% when NII tax is taken into account. The tax on NII brings the highest aggregate federal rate on long term capital gains to 23.8%. State and local income taxes are assessed on top of that.

c. Tax Base

(1) For individuals, tax base is the lesser of:

(a) NII for taxable year, and

(b) the excess (if any) of:

1) the modified adjusted gross income for such taxable year, over

2) the threshold amount.

(c) “Modified adjusted gross income” is adjusted gross income increased by the amount by which the individual’s foreign earned income exceeds
deductions (or exclusions disallowed) attributable thereto.

(d) The “threshold amount” is:

1) $250,000 for married couple filing jointly;

2) $125,000 for married taxpayer filing separately; and

3) $200,000 for any other individual taxpayer.

(2) For trusts and estates, tax base is the lesser of:

(a) the “undistributed NII” for taxable year, and

(b) the excess (if any) of:

1) the adjusted gross income (as defined in section 67(e)) for such taxable year, over

2) the dollar amount at which the highest bracket in section 1(e) begins for such taxable year.

(c) For 2015, trusts and estates reach the highest tax bracket under section 1(e) at $12,300 of taxable income.

(3) Mechanism for determining base amount effectively excludes many individual taxpayers. Tax is targeted at “high income” taxpayers. But it doesn’t exclude many trusts—low dollar threshold for top bracket means most trusts will be subject to tax on NII.

d. Deductions – (the “N” in NII)

(1) Investment income is net of deductions attributable to production of NII.

(2) Note that these are not new NII-specific deductions; they are deductions otherwise available under income tax code, but connected to NII.

e. Net Investment Income (NII)

(1) Key categories of NII
(a) Gross income from:

1) Interest
2) Dividends
3) annuities (non-retirement)
4) royalties
5) rents

(b) Net gain attributable to the disposition of property (other than property held in trade or business not subject to tax on NII)

(c) Gross income derived from passive activity

(d) Gross income derived from business of trading in financial instruments or commodities (as defined in section 475(e)(2) and discussed in Treas. Reg. §1.1411-5)

(e) Gross income derived from investment of active business’s working capital

(2) Income excluded from NII

(a) Income derived in the ordinary course of a trade or business other than (a) a passive activity or (b) a trade or business of trading in financial instruments or commodities

(b) Distributions from qualified plans and IRAs (§1411(c)(5))

(c) Tax-exempt income

B. Floor on itemized deductions:

1. For taxpayers whose adjusted gross income exceeds a threshold amount in 2015 of $309,900 for married taxpayers filing jointly or $258,250 for single taxpayers, a floor is now imposed on total itemized deductions.

   a. In 2015 floor is the lesser of:

      (1) 1 percent of AGI over the threshold amount.

      (2) 80% of the allowable deductions.
b. floor is imposed after all of the other limits on deductions.

c. deductions for medical expenses, casualty losses and investment interest are not included for purposes of computing the floor.

d. deduction for charitable contributions is subject to the new floor.

e. As a result, a taxpayer who has adjusted gross income in excess of $309,900 in 2015 will see itemized deductions reduced by 3 percent of the amount by which adjusted gross income exceeds $309,900. For example, a taxpayer with adjusted gross income of $400,000 and $50,000 of itemized deductions will lose the first $2,703 of those itemized deductions. However, if the taxpayer has only $2,000 of itemized deductions, he or she would lose only the first $1,600 of deductions (80 percent of $2,000) because the new limit cannot reduce the itemized deductions by more than 80 percent.

2. Floor on deductions complicates the issue, but should not adversely impact tax incentive for making charitable contributions for most donors.

a. Most taxpayers with AGI in excess of $309,900 will have deductions for state taxes and/or home mortgage interest in excess of the floor.

b. Since the expenditures for state and local taxes and home mortgage interest are, in most cases involuntary, the floor is absorbed by those expenditures.

   (1) The deductions for home mortgage interest and state taxes are politically sensitive.

   (2) The floor was, in effect, an attempt to reduce the value of these deductions for wealthy taxpayers while not tackling the issue head on.

c. Assuming that the floor is absorbed by the involuntary expenditures for state and local taxes and home mortgage interest, a voluntary decision to make a charitable contribution can be made without taking into account the effect of the floor.

C. Personal exemptions are phased out for high income taxpayers.

1. In 2015, personal exemptions are phased out for high income taxpayers ($309,900 for joint filers, $284,050 for heads of household, $258,250 for single filers) for 2008. These amounts are indexed and adjusted annually.
2. The phase out is tied directly to AGI and is accomplished by direct loss of exemptions.

V. Valuation of Contributed Property; Appraisal Rules.

A. Appraisal rules

The 1984 Act effected dramatic changes in appraisals of property contributed to charitable organizations. Following the scandal involving gifts by taxpayers of gemstones to the Smithsonian Institution which in some cases yielded deductions based on values representing five times the purchase price paid months earlier, Congress acted by directing the Internal Revenue Service to adopt rules to tighten the appraisal process. See Anselmo v. Commissioner, 80 T.C. 872 (1983).

1. Rules adopted by regulation

   a. Regulation Section 1.170A-13(c) requires any individual, C corporation, closely-held corporation, personal service corporation, partnership or S corporation making contributions of property, other than publicly traded securities, deducting a gift to the extent of $5,000 or more ($10,000 for gifts of non-publicly traded securities) to obtain a qualified appraisal. The qualified appraisal must be obtained and an “appraisal summary” must be attached to the donor’s federal income tax return. The qualified appraisal must be made not more than 60 days prior to the date of the gift or at any time after the gift up to the date of filing of the donor’s federal income tax return. The appraiser may not be an employee or relative and may not be a party to the transaction in which the donor acquired the property, in other words, a dealer who sold property to the donor, unless the property is contributed within two months of the date of acquisition and the appraised value does not exceed the acquisition price. The qualified appraiser may not be the donee of the property, or any person whose relationship to any of the previously listed persons would cause a reasonable person to question the independence of the appraiser.

   b. IRS Publication 561 (Rev. April 2007) entitled Determining the Value of Donated Property discusses valuation of many different types of contributed assets.

2. Appraisal Summary - Form 8283

The appraisal summary is made on Form 8283. One Form 8283 must be completed for each item or group of “similar items” and attached to the donor’s federal income tax return for the year in which the deduction is first claimed. The appraisal summary must be prepared, signed, and dated
by the appraiser. It must also be signed and dated by the donee to acknowledge receipt of the appraised property.

a. In the case of a gift to a charitable remainder trust in which the donor is himself the trustee, the appraiser signs and completes the Form 8283 and then turns over that form to the donor who in his capacity as trustee also acknowledges receipt of the appraised property. If the donor, John Jones, has made his gift to the John Jones Charitable Remainder Trust, he, in his capacity as trustee of that trust, serves as donee, and must acknowledge receipt of the appraised property on the Form 8283.

b. Any gift of art such as a painting, sculpture, water color, or print must be documented on Form 8283 by a photograph. If the aggregate value is $20,000 or more according to the instructions for the Form 8283, a copy of the appraisal itself, not merely the appraisal summary, must be attached to the donor’s income tax return.

c. Taxpayers may now request from the IRS a “Statement of Value” that can be used to substantiate the value of art for income, estate, or gift tax purposes. The procedures for requesting the Statement of Value are found in Revenue Procedure 96-15. In order to use the procedure, the item of art must have been appraised independently at $50,000 or more. A user fee of $5,400 for the first three items to be included in the Statement of Value, plus $270 for each additional item is charged by the IRS. The term “art” is defined broadly by the Revenue Procedure and includes, inter alia, paintings, sculpture, rare manuscripts and historical memorabilia.

d. If a deduction of more than $500,000 is claimed, the donor must not only obtain a qualified appraisal and but also must attach the appraisal to its tax return. Failure to obtain the appraisal and to attach the Form 8283 to the donor’s federal income tax return will cause the donor to lose his income tax deduction completely. An exception is made only if the failure can be shown to be in good faith and the Form 8283 or appraisal summary is furnished to the Internal Revenue Service within 90 days after the Internal Revenue Service request it. Failure to obtain the appraisal (not to be confused with the appraisal summary) means loss of deduction regardless of good faith. Overappraisal also results in serious penalties.

e. In Bond v. Commissioner, 100 T.C. 32 (1993) the donors had contributed two blimps to charity without obtaining an appraisal and attached the Form 8283 to the Form 1040. The Tax Court held
that the donors had substantially complied with the appraisal requirements.

f. What kind of property must be appraised? Every kind of property having a fair market value in excess of $5,000 other than marketable securities. The limitation is increased to $10,000 in the case of non-publicly traded securities. In other words, the appraisal rules apply to insurance policies (in which case a difficult question arises as to who may perform the appraisal), valuable coins (even though they may be legal tender), closely-held stock, real estate, tangible personal property, partnership interests among others.

g. The appraisal rules do not apply to gifts of publicly traded securities. In typical fashion, the definition provided by the regulations is circuitous -- non-publicly traded stock is stock which is not publicly traded. Publicly traded securities are those for which market quotations are readily available on an established securities market. See Reg. Sec. 1.170A-13(c)(7)(xi).

(1) “Publicly traded” means regularly traded on a national, regional, or over-the-counter market and includes shares of an open ended investment company or mutual fund for which quotes are published daily in the newspaper. If the market value is only available through an interdealer quotation system, the stock is publicly traded provided it meets five rules set out in that regulation, relating to maintenance of records and availability of information.

(2) Even though the stock may meet the definition of publicly traded securities, if a block of stock given is so large that a discount would be applied in the event of a sale, in other words a blockage situation, then the stock is not publicly traded, states Reg. Section 1.170A-13(c)(7)(xi)(C). If the contributed securities are restricted with respect to sale, in other words, if SEC Rule 144 would limit sales in any particular quarter, then these shares may not be readily marketable; however, the regulation does not deal precisely with this point.

h. PLR 9247018 described a gift by a taxpayer of 5.5 percent of the stock of corporation traded on the New York Stock Exchange. Because of Securities and Exchange Rule 144 the donor was prevented by restrictions temporarily blocking its sale from selling or exchanging the stock before a certain transfer date. Prior to that date, the donor made a gift of the stock to a private foundation.
(1) Section 170(e)(5) allows a full fair market value deduction for gifts of “qualified appreciated stock” to certain non-operating private foundations. “Qualified appreciated stock” is defined to mean stock that is “capital gain property” and “for which (as of the date of the contribution) market quotations are readily available on an established securities market.” If the contributed stock failed to meet the definition of qualified appreciated stock, the donor would be limited to his tax basis or cost for the deductibility of the gift, whereas if the gift were of qualified appreciated stock, he would obtain the deduction for the full fair market value.

(2) The language of Section 170(e)(5) is similar to the language of Reg. Section 1.170A-13(c) which requires an appraisal of securities other than “publicly traded securities”, defined as “securities for which (as of the date of the contribution) market quotations are readily available on an established securities market.” The Regulations repeat this definition but go on to provide that securities are not considered publicly traded securities if, inter alia, “the securities are subject to any restriction that materially affects the value of the securities to the donor, or prevent the securities from being traded”. See PLRs 9247018, 9441032 and 9623018.

i. Form 8283 asks the charitable donee to state whether the donee intends to use the property for unrelated purposes. If the charity answers “Yes,” the donor knows that her deduction will be limited to her basis, assuming that is less than fair market value.

j. If the charitable recipient (or trustee if the donor is a charitable remainder trust or pooled income fund) disposes of the contributed property within two years of the gift, it must report the sale price on the Form 8282. The Form 8282 must be filed with the Internal Revenue Service within 125 days of the date of disposition and a copy must be submitted to the donor. The Form 8282 enables the Internal Revenue Service to cross-check the valuation because that form discloses the donor’s name and the taxpayer identification number.

B. Stricter Rules Adopted in 2006 by the PPA for Appraisal and Appraiser

1. The PPA now requires appraisers to provide a statement of their qualifications in the appraisal itself, in addition to the existing requirements that the appraiser demonstrate education and experience in valuing the type of property fairly appraised and has not been banned from

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practice before the IRS. The IRS has issued a written notice stating that, to meet the PPA requirements, the appraiser must have earned an appraisal designation from a recognized appraiser organization or have otherwise met minimum education and experience requirements and the appraiser must regularly perform appraisals for which he or she receives compensation. The PPA imposes new penalty provisions are imposed on appraisers who prepare appraisals resulting in substantial or gross valuation misstatements of value in connection with a tax filing.

2. Lower thresholds for imposing accuracy related penalties on income tax returns. Under the new law, a substantial valuation misstatement exists when the claimed value of any property is 150% or more of the amount determined to be the correct value. Code Section 6662(e)(1)(A). A gross valuation misstatement occurs when the claimed value of any property is 200% or more of the amount determined to be the correct value. Code Section 6662(h)(2)(A).

3. Lower thresholds for imposing accuracy-related penalties on estate and gift tax returns. A substantial estate or gift tax valuation misstatement now exists when the claimed value of any property is 65% or less of the amount determined to be the correct value. Code Section 6662(g). A gross estate or gift tax valuation misstatement exists when the claimed value of any property is 40% or less of the amount determined to be the correct value. Code Section 6662(h)(2)(C).

4. Scope of reasonable cause exception reduced. Under the new law, the reasonable cause exception to the accuracy-related penalty does not apply in the case of gross valuation misstatements made with respect to charitable deduction property. Code Section 6664(c)(2).

5. Civil penalties on appraisers. The Act establishes a civil penalty on any person (e.g., an appraiser) who prepares an appraisal that is to be used to support a tax position if the appraisal results in a gross valuation misstatement or, in the case of chapter 1 of the Code (income taxes), a substantial valuation misstatement. Code Section 6695A. The penalty is equal to the greater of $1,000 or 10% of the understatement of tax resulting from a substantial or gross valuation misstatement, up to a maximum of 125% of the gross income received by the appraiser for preparing the appraisal. The penalty will not apply if the appraiser establishes that it was “more likely than not” that the appraisal was the proper value. It is not intuitively obvious how an appraiser might take advantage of this defense given that the penalty is assessed after a finding of a substantial or gross valuation misstatement. The Act also gives the Secretary of the Treasury wider latitude to discipline appraisers and does not require that a civil penalty for “aiding and abetting” a tax understatement under Code Section 6701 be assessed before disciplinary proceedings are instituted. This new provision has wider implication than
charitable gifts and would apply, for example, to an appraisal of a partnership interest for gift or estate tax purposes that involves a gross valuation misstatement.

6. Definitions of “Qualified Appraisal” and “Qualified Appraiser”. The Act revises the definitions of both a “qualified appraisal” and a “qualified appraiser” for purposes of the substantiation and documentation requirements for charitable contributions of property valued at more than $5,000, and for the reasonable cause exception to the underpayment penalty provisions. A qualified appraisal is defined as an appraisal that is treated as such under regulations and conducted by a qualified appraiser under generally accepted appraisal standards. Code Section 170(f)(11)(E)(i). The definition of qualified appraiser is now codified and means an individual who: (1) has earned an appraisal designation from a recognized professional appraisal organization or has otherwise met minimum education and experience requirements to be determined by the IRS in regulations; (2) regularly performs appraisals for which he or she is compensated; (3) has verifiable education and experience in valuing the type of property for which the appraisal is being performed; (4) has not been prohibited from practicing before the IRS for the three years prior to the appraisal; and (5) meets other requirements prescribed in regulations or other guidance. Code Section 170(f)(11)(E)(ii) and (iii). Accordingly, it is no longer sufficient that the appraiser hold himself or herself out to the public as an appraiser or perform appraisals on a regular basis.

7. Effective Date. The accuracy-related penalty provisions apply to returns filed after August 17, 2006. The provision establishing a civil penalty that may be imposed on any person who prepares an appraisal that is to be used to support a tax position if such appraisal results in a substantial or gross valuation misstatement applies to appraisals prepared with respect to returns or submissions filed after August 17, 2006. The provisions relating to appraiser oversight (penalties and discipline) apply to appraisals prepared with respect to returns or submissions filed after August 17, 2006.

VI. Acknowledgment of Charitable Gifts and Quid Pro Quo Rules

A. Substantiation rules

1. The 1993 Act included stringent reporting requirements for donors and charities making or receiving gifts of as little as $75. Sections 170(f)(8) and 6115.

B. Acknowledgment

1. Any contribution of $250 or more is not deductible for federal income tax purposes unless the donor has an acknowledgment from the charitable
organization. In addition to the name of the organization, the acknowledgment or receipt must contain three items:

a. the amount of cash contributed or, in the case of a noncash contribution, a description (but not a valuation) of the property contributed,

b. a statement of whether or not the charitable donee provided any goods or services to the donor in consideration for the contribution, and

c. if any goods or services were provided, a description and good faith estimate of the fair market value of the goods or services provided.

2. The acknowledgment may be made by letter, postcard, computer generated form, or, appraisal according to Publication 1771, Charitable Contributions – Substantiation and Disclosure Requirements, revised July, 2013.

3. Only gifts which are deductible for income tax purposes are affected. Gifts by private foundations and decedents’ estates are not affected. Intangible religious benefits or incidental benefits such as increased name recognition need not be valued.

4. While any single contribution of less than $250 technically does not require acknowledgment, as a practical matter, an individual who has given the organization more than $250 over the course of the calendar year in two or more gifts will at tax preparation time be anxious to have a receipt to protect the deductibility of the gift.

5. The receipt is timely if provided not later than the date of filing of the donor’s federal income tax return for the year of gift, including all extensions. As a practical matter, individual donors will generally expect receipts by January 31st of the year following the year of gift in order to prepare their returns or to give their tax information to their tax preparers. Corporate and other donors who file tax returns on a fiscal rather than calendar year basis will need acknowledgments before returns are filed. Corporate donors should receive acknowledgments within 60 days following the date of a contribution.

6. The substantiation requirements will not apply if the charity files an information return with the IRS, reporting the deductible value of particular contributions. Forms of reporting have not yet been developed by the IRS to allow charities to report gifts of $250 or more, but since the burden is on the donor to obtain the acknowledgment in order to be
entitled to a deduction, a donor might be reluctant to rely on the charity’s assurance that such a form has been filed.

a. In general, separate contributions to the same organization will not be aggregated for purposes of the $250 threshold. For purposes of payroll deductions, each such deduction represents a separate gift. Reg. § 1.170A-13(b) provides that a contribution made by withholding from a donor’s wages may be substantiated with (i) a paystub, Form W-2, or other document showing the amount withheld, and (ii) a pledge card or other document prepared by the donee client, stating that no goods or services were provided in exchange for contributions made through payroll deductions.

7. A charity such as a United Way or community foundation may receive a contribution from a donor and distribute that contribution, whether pursuant to a donor’s instructions or otherwise, to one or more charities as ultimate recipients. In that case, the original charitable recipient will be treated as the donee for acknowledgment purposes.

C. Quid Pro Quo Disclosure

To ensure that donors do not deduct contributions when goods or services are received in return, the 1993 Act requires a charity which provides goods or services to the donor in return for a contribution of more than $75 made on or after January 1, 1994 to furnish the donor with a written statement indicating a good faith estimate of the value of the goods or services so provided. A specific disclosure either on the solicitation or receipt for the contribution must inform the donor that the deductible portion of the contribution is limited to the excess of the contribution over the value of the goods or services received in return. Section 6115.

1. While a fund-raising event with the ticket price of, for example, $50 for which the quid pro quo is $30 would not technically fall within the $75 disclosure rule, many donors will buy two or more tickets.

2. Whenever an individual donor expends more than $75, even though it is for several tickets, the disclosure is required; therefore, it is advisable to include the disclosure on all solicitations regardless of amount to avoid the need for a special disclosure for a donor who buys multiple tickets. See 1994 (for FY 1995) Exempt Organizations Continuing Professional Education Technical Instruction Program Textbook including a chapter by Bloom and Jones, “Substantiation and Disclosure rules of OBRA ‘93, p. 129, 135.

3. While there is technically no penalty on the charity for failure to provide the acknowledgment to a donor of $250 or more, the donor will not be
entitled to the deduction. A penalty may be imposed on a donee charity, which fails to comply with the *quid pro quo* disclosure requirement calculated as $10 for each contribution for which the disclosure requirement is violated. Section 6714.

4. Revenue Procedure 90-12, specifically referenced in the commentary introducing the final regulations issued in connection with the 1993 Act and Reg. §§ 1.170A-1(h) and 1-13(f) clarify the treatment of low cost articles distributed in connection with the fundraising solicitation. The safe harbor created by the Revenue Procedure protects certain de minimis *quid pro quo* payments.

   a. If a contribution occurs in the context of a fundraising campaign and the charity gives the donor a modest thank you either in the form of a gift such as an umbrella or an invitation to an event and the fair market value of all benefits received by the taxpayer does not exceed the lesser of 2 percent of the payment or $105 (in 2015 indexed for inflation), the quid pro quo may be ignored.

   b. For example, a donor making a gift of $1,000 may not receive a benefit in excess of 2 percent or $20. If the only benefits received are “low-cost items” such as bookmarks, calendars, keychains or mugs bearing the organization’s name or logo the cost of which to the charity does not exceed a low cost limit, again the quid pro quo may be ignored. A donor making a gift of $52.50 (in 2015) may receive a gift of a low-cost article having a value of $10.50 in 2015.

5. In this connection, as with any other *quid pro quo* provided by the charity to a donor, it is irrelevant that the low-cost articles were donated to the charity. Rather, the charity is obligated to make a reasonable estimate of the amount which it would have to pay for the articles if it had purchased them. The donor’s deduction must be reduced accordingly.

6. The charity may always advise a donor in writing that the donor has the right to decline any goods or services which the charity may provide in consideration for the gift. If the donor declines the invitation to an acknowledgment dinner or other *quid pro quo*, the donor should be permitted the full deduction for the gift. If the donor accepts the invitation but does not attend, the donor must nevertheless be advised that the deductible gift is reduced by the value of the dinner since the donor had the right to attend, even though that right was not exercised.

7. If a donor gives food or wine to a charitable organization in connection with a fundraising event. The food or wine would constitute tangible personal property not given for exempt purposes; therefore, the donor’s deduction is limited to tax cost or basis. Reg. § 1.170A-4. The donor is
entitled to deduct his out-of-pocket expense as a charitable gift. If a donor gives services to a charity, she is not entitled to any deduction for the value of the services. Nevertheless, the value of those services, if used to induce a gift, must reduce the purchaser’s deduction. For example, a donor-cook might offer to a charity auction a dinner to be cooked for 10 people, and an enthusiastic auction participant may purchase the dinner for $2,000. If the charity has agreed with the donor in advance that the value of the dinner is $50 per person or $500 total and has stated that in the auction catalogue, the purchaser should be entitled to a deduction for $1,500 or the difference between the amount of his payment and the quid pro quo received. The donor may deduct only his out-of-pocket costs in connection with the dinner, not the value of his services. If it is impossible to value the item purchased, the presumption is that no gift has been made by the purchaser at all.

8. While most charities have adopted procedures for acknowledging and estimating the value of the quid pro quo for any goods or services given in return for a contribution, some charities may need to restructure their fundraising programs. For example, a college that rewards “President’s Associates” who contribute more than $10,000 with a fancy dinner with the president may decide that, rather than trying to estimate the value of the right to attend a free dinner for all President’s Associates, it is simpler just to give those President’s Associates who want to have dinner with the president the right to pay for the cost of that dinner.

D. Criteria for Deductibility

Reg. § 1.170A-13(F) and Reg. § 1.6115-1 create a two-part test for determining whether a donor may claim a deduction for his charitable contributions. To claim a deduction for a charitable contribution, the donor must both intend and actually make a payment in an amount that exceeds the fair market value of any goods or services received in return.

E. Quid Pro Quo Contributions

1. When calculating the deduction allowed for quid pro quo contributions, donors and donees are already permitted to disregard goods or services that are treated as having insubstantial value under existing IRS guidelines ($10.50 in 2015, plus newsletters unless they are of commercial quality and other benefits worth two percent or less of a payment up to a maximum of $105 for 2015). Other benefits may be disregarded if they are given as part of an annual membership offered in return for a payment of $75 or less and fall into one of two categories. The first is admission to events that are open only to members and in which the donee organization reasonably projects that the cost per person will be equal to or less than the low cost amount ($10.50 for 2015). The second and more significant category consists of rights or privileges that members may exercise
frequently during the membership period, such as free admission to a museum.

2. The regulations recognize the difficulty in valuing membership benefits such as free or discounted admissions, parking, and gift shop discounts whether provided by donee, for example, in the museum gift shop or by merchants in the community upon a showing of organization membership. (Many public television/radio stations offer a membership for $75 or less which entitles the member to discounts at local coffee shops, music stores, and the like. These membership benefits may be ignored to the same extent as if they were provided directly by the recipient charity.) As a result, if the payment is $75 or less and the only benefits provided to members are frequently exercised rights or privileges, the entire amount may be treated by the donor and acknowledged by the donee as a charitable contribution. This provision is of considerable benefit to museums and membership organizations. Such *de minimis* benefits may also be disregarded if provided to the donor’s employees.

3. The regulations provide relief to a donee organization which receives matching gifts. For example, when a matching gift is made by an employer, any goods or services provided by the donee will be treated as purchased by the employee. The employer would then receive a full charitable deduction while the employee’s deduction would be reduced by the *quid pro quo* received. A donee organization is permitted to use any reasonable method (not necessarily the highest value) in determining the fair market value of goods or services provided in exchange for a transfer.

4. The value of items purchased at a charity auction will not be presumed equal to the payment received if the charity has reasonably established a lower value in advance. In other words, if a donor buys a work of art for $500 at a charity auction but the artwork has been valued and listed in a catalogue published in advance as worth $150, the donor has made a gift of $350. The donor should receive an acknowledgment which states that the donor has made a gift of $500 and has received goods worth $150 in exchange for the gift. The presence of a celebrity at an event adds no value to what a donor receives unless the celebrity provides a service for which he or she is typically paid. A tennis lesson provided by prominent tennis professional purchased by a donor for $500 when the professional typically charges $100 for the lesson would result in a gift to the charity of $400, which should be appropriately acknowledged by the charity. A museum tour by the tennis professional, by contrast, shall be deemed to have no value. If any intangible religious benefits are provided, they may be disregarded for valuation purposes but a statement that such benefits have been provided is required.

5. Goods or services provided in exchange for a payment by a donor must be valued in accordance with the *quid pro quo* rules even though they may be
provided in a year earlier or later than the year in which the taxpayer makes the payment to the donee. In other words, a gift which the donor knows will entitle him to an invitation in the following year to a special President’s dinner must be reduced by the value of the dinner. If a donor can be given an option of accepting or rejecting the dinner or other anticipated benefit by, for example, returning a postcard to the donee saying “I do not wish to receive an invitation to dinner. Thanks.”, the donee may acknowledge the full amount of the donor’s gift without reduction for any *quid pro quo*, unless the donee accepts the benefit by returning the postcard.

6. The issue of intangible religious benefits poses a particularly difficult problem under the general rubric of the *quid pro quo*. Section 170(f)(8)(B)(iii) states that goods or services given in exchange for a gift need not be treated as a *quid pro quo* if they consists solely of “intangible religious benefits...,” although a statement that such benefits have been provided is required. An intangible religious benefits is then defined as one “provided by an organization organized exclusively for religious purposes and which generally is not sold in a commercial transaction outside the donated context.” No other guidance is provided. However, empirical evidence suggests there is a substantial lack of uniformity as to how various payments to religious organizations are treated even within the same denomination. Many religious organizations provide benefits to congregants which, although they may be part educational, are in fact primarily religious in nature. For example, a church may offer a Sunday School or bible study class or a synagogue may provide Bar Mitzvah classes to congregants. A distinction might reasonably be implied between those intangible religious benefits provided to congregants rather than to the public at large so long as no curricula educational requirement is fulfilled or credit or degree awarded in connection with such class.

7. Transfers to Deferred Gift Vehicles

Transfers to charitable remainder or lead trusts need not be acknowledged by any donee charity or trustee since the charitable donee may be undesignated, or if designated, the donor may have reserved the right to change the designation prior to the termination of the trust. Gifts to pooled income funds are made to a charity which must be designated; therefore, such gifts must still be acknowledged. A charitable gift in exchange for a gift annuity must still be acknowledged by the charitable organization as a *quid pro quo* gift, as described above, since the transfer represents part gift, part purchase of an annuity.

8. Unreimbursed Volunteer Expenses
Unreimbursed expenditures incurred by a taxpayer incident to the rendition of services to a donee charity have always been deductible. The Section 170 regulations recognize the difficulty of substantiating such expenses and provide that where the donor has incurred individual unreimbursed expenditures in volunteering services, the expenditures may be substantiated by the donor’s normal records consistent with the business expense rules (requiring receipts and information regarding the nature of the volunteer activity) and an abbreviated written acknowledgment provided by the donee organization containing a description of the services provided, whether or not the donee provided any goods or services in exchange, or if the donee provided any goods or services, a good faith estimate of the value of those goods or services. In other words, a volunteer who incurs $1,000 of travel expenditures in connection with soliciting contributions from his college classmates in anticipation of a reunion gift may deduct his expenses provided he adequately documents his travel and obtains an acknowledgment from the college describing the nature and date of the fundraising activity, whether any goods or services were provided in exchange for the volunteer’s services (such as a thank-you present) and the value of any such quid pro quo. Reg. § 1.170A-13(f)(10).

9. Payments For the Right to Purchase Tickets to College Athletic Events

The regulations contain language specifically addressing payments made to obtain “points” or other status with a college athletic boosters group. Reg. § 1.170A-13(f)(14). With respect to a donor who obtains the right to purchase tickets to college or university athletic events, Section 170(1) provides that 20 percent of any such payment is treated as non-deductible while the remaining amount is deductible in full, regardless of the nature of the tickets that may be purchased. The final regulations clarify that for purposes of the quid quo pro rules, this 20 percent figure is deemed to equal the fair market value of the right to purchase the tickets. (Note: In addition to the 20 percent payment that is non-deductible, the donor must also pay the cost of the tickets.) Section 170(1) can be a “trap for the unwary” for schools utilizing a “point” system that rewards substantial donors with the right to purchase premium seats. Under such systems, careful planning is necessary in order to avoid having such donors lose the tax deductibility of 20 percent of a very large gift, simply because they are permitted to purchase seats that are only marginally better than those that may be purchased by virtue of a much smaller contribution.

F. 2006 PPA Substantiation Requirements.
1. Limits on and substantiation requirements for donations of clothing and household items

Effective after August 17, 2006, no charitable deduction will be allowed for gifts of clothing or household items (not including food, paintings, antiques, other art objects, jewelry, gems or collections) unless the items are in “good used condition or better”. Code Section 170(f)(16). The IRS may also by regulation deny a deduction for such a gift if it has minimal monetary value. However, if the deduction claimed for a single donated item is greater than $500 and a qualified appraisal is included with the taxpayer’s return, a deduction may be permitted, notwithstanding the condition of the contributed item.

2. Cancelled check or receipt required for charitable contributions of money

Under Code Section 170(f)(8), a taxpayer is required to substantiate any charitable gift of $250 or more by obtaining a contemporaneous written acknowledgement from the charitable donee that describes the amount of cash or the property donated and that states whether the charity has provided any goods or services in exchange for the gift. This provision remains in place under the Act. For all cash contributions (regardless of amount), the donor can satisfy recordkeeping requirements only by maintaining as a record of the contribution either a bank record or a written communication from the donee showing the name of the donee organization and the date and amount of the contribution. If these records are not kept for a particular donation, no deduction is allowed for that donation. Code Section 170(f)(17). This change in the law effectively eliminates the deductibility of anonymous small cash gifts, such as cash contributed to a church collection plate or a Salvation Army kettle.