32nd Annual Representing and Managing Tax-Exempt Organizations Primer on Charitable Contributions

Carolyn M. Osteen©
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Income Tax Deduction For Charitable Gifts

• The percentage limitations for income tax deductions for charitable contributions by individuals
  – Basic limit: 50% of taxpayer’s “contribution base” IRC § 170(b)(1)(A)
  – 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.
  – 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).
  – 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
Income Tax Deduction For Charitable Gifts (cont’d)

- First 30 percent sublimit. § 170(b)(1)(B); private foundations, etc.
- Second 30 percent sublimit: gifts of “capital gain” property. § 170(b)(1)(C)
- Gifts of S Stock
- Charitable Split Dollar Life Insurance, Annuity and Endowment Contracts
- Charitable Contributions Cars, Boats, and Planes and of Patents and Other Intellectual Property
- Gifts of Fractional Interests in Tangible Personal Property.
- Recapture Rule for Certain Donations of Tangible Personal Property
- Charitable Contributions of Taxidermy
Income Tax Deduction For Charitable Gifts (cont’d)

• Expired Charitable Giving Incentives Adopted in the PPA of 2006
  – IRA Rollover
  – Enhanced deduction for conservation contributions
• Planning with the income tax deduction limits
Income Tax Deduction - limits on gifts by corporations. § 170(b)(2)

- Corporations are generally subject to a simple limit of ten percent of taxable income.
- 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.
- As with individuals, corporations are allowed a five year carryover for contributions that exceed the limit.
- Capital gain property and § 1231 property are deductible at fair market value; all other property (e.g., inventory) is deductible at basis.
- Special rules for contributions of inventory.
- Charitable Contributions of Food and Book Inventory Enhanced by the Katrina Emergency Tax Relief Act of 2005.
Income Tax Deduction - limits on gifts by corporations. § 170(b)(2) (cont’d)

- 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).

- PPA Changes to Basis of S Corp. Holdings
The percentage and other limitations contained in § 170(b)(1) apply only to individuals and relate to the deduction taken under § 170(a).

§ 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.

Thus, trusts and estates are allowed a charitable income tax deduction limited only by gross income; no need for carryover.
Impact of Recent Legislation on Charitable Contributions

• Changes in the top rate:
  – 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.
Impact of Recent Legislation on Charitable Contributions (cont’d)

• Key Concepts and Mechanics
  – Applicability
    • Tax on NII is intended to apply to:
      • Individual taxpayers; and
      • Trusts and estates

• Tax Rate
  – Tax is assessed at 3.8%
    • 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.
Impact of Recent Legislation on Charitable Contributions (cont’d)

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

• Personal exemptions are phased out for high income taxpayers
  – 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.
  – The phase out is tied directly to AGI and is accomplished by direct loss of exemptions.
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).
• Rules adopted by regulation
  – 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.
Valuation of Contributed Property; Appraisal Rules (cont’)

• Appraisal Summary – Form
  – Stricter Rules Adopted in 2006 by the PPA for Appraisal and Appraiser
Acknowledgment of Charitable Gifts and Quid Pro Quo Rules

• Substantiation rules
  – 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.

• Acknowledgment
  – 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:
    • the amount of cash contributed or, in the case of a noncash contribution, a description (but not a valuation) of the property contributed, and
    • a statement of whether or not the charitable donee provided any goods or services to the donor in consideration for the contribution, and
Acknowledgment of Charitable Gifts and Quid Pro Quo Rules (cont’d)

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

• 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.
• Criteria for Deductibility Quid Pro Quo Disclosure
  – 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.

• Quid Pro Quo Contributions
  – 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.
Acknowledgment of Charitable Gifts and Quid Pro Quo Rules (cont’d)

- Unreimbursed Volunteer
- Payments For the Right to Purchase Tickets to College Athletic Events

- 2006 PPA Substantiation Requirements
  - Limits on and substantiation requirements for donations of clothing and household items
  - Cancelled check or receipt required for charitable contributions of money