Jen Wickham - Fri, 11/1/2013 - 13:51

The largest asset owned by many prospects is their home. A gift plan defined by federal tax law that allows an individual to donate her home or farm to a charity while retaining the right to live in it for the rest of her life.

The donor irrevocably deeds her home or farm to the charity, but retains the right to live in it for the rest of her life, a term of years, or a combination of the two. The donor may also use a vacation home to create this kind of gift. The donor receives an income tax deduction for the remainder value of the home to the charity, subject to IRS 30%/50% limitations.

While the donor retains the right to live on the property, she continues to be responsible for all routine expenses - maintenance fees, insurance, property taxes, repairs, etc. If the donor later decides to vacate the property, she may rent all or part of the property to someone else or sell the property in cooperation with charity.

When the retained life estate ends, the charity can then use the property or the proceeds from the sale of the property for the purpose the donor designates.

A retained life estate (RLE) allows a donor to give title to her home while retaining the right to live in it for life. In return, she receives a current charitable deduction and unlocks a valuable asset for the benefit of your charity. To make the arrangement more attractive for the donor, some charities will offer a gift annuity in exchange for the RLE so that the donor can enjoy some new income.

Fearing that the net sales proceeds may be substantially less than the appraised value, some charities offer to pay an annuity equal to the published rate for a person of the annuitant’s age multiplied by the net sales proceeds. Sometimes they delay executing the gift annuity agreement until the property is sold, and they indicate on Schedule A of the gift annuity agreement that the
value of the property contributed was the net sales proceeds. In an IRS audit, it may appear that the donor sold the property, with the charity acting as agent, and then contributed the net proceeds. If that were the conclusion, the charitable deduction would stand, but the donor might be taxed on all of the capital gain in the property in the year it was sold.

The safest way to proceed is to make a conservative estimate of the net proceeds to be realized and offer a gift annuity rate equal to:

estimated net proceeds divided by the appraised value multiplied by the normal gift annuity rate appraised value

This results in discounting the gift annuity rate, and, of course, the donor should consent to the discount through some written instrument. It is the rate, not the property value, that should be discounted, for the value of the property reported on Schedule A of the gift annuity agreement should be the same as the value determined by the appraisal and entered on Form 8283. The financial consequences to the charity are the same whether the property value is discounted 10 percent or whether the gift annuity rate is discounted 10 percent.

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