Bill Laskin - Sat, 6/20/2015 - 13:10

A donor who is thinking of making certain gifts during life needs to pay attention to various requirements to ensure he can claim an income tax charitable deduction. When the same gifts are made upon death, however, these same requirements do not apply – or at least not in the same way.

AGI Limitations Don't Apply

Although a donor's estate can become subject to income taxation in connection with *income* it receives, charitable gifts from the donor's estate typically are made with *assets* of the estate and thus do not affect the estate's income tax situation. Of course, if the value of those assets is more than the $5.43 million gift and estate tax exemption available in 2015 (and indexed for inflation in future years), the estate will need to take the federal estate tax – a form of transfer tax – into account. The threshold for this tax is so high, however, that it will affect the estates of far fewer than one percent of those who die each year. Nevertheless, because approximately two dozen states have state estate taxes, and because most of those states have thresholds substantially smaller than the federal threshold, state estate taxation may become relevant even when federal estate taxation is not.

Fortunately, a general principal of estate taxation is that deductions for charitable gifts can be claimed without limitation. In other words, the 50-, 30-, and 20-percent of adjusted gross income (AGI) limitations that apply to income tax charitable deductions do not apply to estate tax charitable deductions. Nor do such limitations apply to the other primary type of transfer tax, the federal gift tax. (Very few states have any sort of gift tax.)

Example: *During life, Chip donates to a charity a $300,000 piece of real estate with a cost basis of $120,000. He purchased the property many years ago, so it is a long-term capital gain asset. Chip's AGI is $100,000.*

If the recipient organization is a public charity, Chip will receive a $300,000 income tax charitable deduction, but he will be able to claim the deduction only up to a limit of 30 percent of his AGI in the year of the gift, plus in each of the five years into which any unused portion of the deduction can be carried forward. Assuming his AGI remains at $100,000 per year throughout these six years, he will be able to claim no

more than $180,000 (i.e., 6 x $30,000, which is 30% of $100,000) of his $300,000 deduction.

If the recipient organization is a private, non-operating foundation, his income tax deduction is limited to his $120,000 basis in the real estate and he can claim the deduction up to a limit of 30 percent of his AGI. Again, assuming his AGI remains at $100,000 per year each year in the future, it would take a total of four years to claim the full $120,000 (i.e., 4 x $30,000, which is 30% of $100,000) amount of his deduction. (If he had contributed long-term appreciated publicly-traded securities instead, his deduction would be the full $300,000 value of the securities, but he would be able to take no more than 20 percent of AGI each year.)

***Note:** In either case, whatever unused deduction is carried forward from one year into the next will be subordinate to deductions associated with charitable gifts made in that carry-forward year.*

By contrast, if Chip's gift is made upon his death, his charitable deduction for the gift will be $300,000, assuming that the property's value remains constant. This will be the case regardless of whether the recipient organization is a public charity or a private, non-operating foundation. In addition, his estate can claim the full amount of the deduction, rather than just some fraction of it. Of course, the availability of this deduction will make a difference only if Chip's estate is worth enough to be subject to federal and/or state estate tax.

Interestingly, the same rules governing a gift for estate tax purposes will also govern for purposes of the federal gift tax if Chip ends up making the gift during his lifetime after all. The gift tax charitable deduction will be $300,000, all of which can be claimed in the year of the gift, and this will be the result regardless of whether the gift is made to a public charity or to a private, non-operating foundation.

Adios, IRS Form 8283 and, Possibly, Appraisals

If an asset other than cash is contributed to charity, whether during life or upon death, the asset's value must be established before the amount of the deduction can be determined. If the deduction claimed for all non-cash contributions exceeds $500, the taxpayer must file a completed Form 8283 with his or her income tax return. In contrast, a donor's executor does not need to complete a Form 8283 (or any similar form) to substantiate an estate tax deduction.

If the asset in question is publicly-traded stock (or certain other types of securities), its value can be determined easily. In the case of most other assets, however, the value may be more difficult to ascertain and possibly require a formal appraisal. To secure an income tax charitable deduction for such assets, a formal, "qualified" appraisal of the asset meeting the requirements of Treasury Regulation Section 170A-13(c)(3) is required if the amount of the deduction exceeds $5,000 ($10,000 in the case of closely-held stock).

For purposes of securing an estate tax charitable deduction or a gift tax charitable deduction, however, valuing a non-cash asset other than publicly-traded securities may or may not require an appraisal. The determination is generally made by tax counsel to the donor or the estate. The amount of the charitable deduction will then be simply the value of the asset in question, so long as:

- no taxes or administrative expenses are payable out of that value;
- in the case of a married donor who dies in certain states, no "marital election" is made against the asset;
- the contribution is made outright, not by means of a life income gift or some other partly charitable, partly non-charitable arrangement (a principle that likewise applies to calculation of a donor's income tax charitable deduction); and
- there are no material restrictions on the gift that result in the benefit to the charity being less than the value of the asset.

Even if a formal appraisal will be required for estate tax or gift tax purposes, IRS Form 8283 will not need to be completed. That form pertains strictly to the substantiation of a federal income tax charitable deduction.

Related-Use Concerns Evaporate for Gifts of Tangible Personal Property
Among the categories of assets a donor might draw upon to make a charitable gift is tangible personal property. Tangible personal property includes any asset you can touch that is not real estate, for example, a boat, a car, jewelry, artwork, or furniture.

A donor who makes a gift of tangible personal property during life must be mindful of how the nature of the property relates to the nature of the charity's mission. Specifically, if the charity can use the property for a purpose or function constituting the basis for the charity's exemption from federal income tax, then *that piece of*

property, with respect to *that particular charity*, is regarded as related-use property.

If the donor has owned such property more than a year, then the donor can claim an income tax charitable deduction for the fair market value of the property, provided the charity is a public charity. If, however, the public charity will not put the property to a related use, then the donor's deduction will be limited to the lesser of the donor's cost basis in the property or its fair market value, regardless of how long the donor has owned the property. Finally, if the property is contributed to a private, non-operating foundation, the donor's deduction will once again be limited to the lesser of the donor's cost basis or the property's fair market value in all instances.

In short, at least from a tax standpoint, a donor wishing to use an item of tangible personal property to make a gift to a charity during life will often be no worse off by simply selling the item and giving the resulting cash proceeds. What's more, upon sale, the donor could decide to give only some of the cash and keep the rest.

These tax considerations will be greatly simplified when a donor's estate gives tangible personal property to a charity. Here again, for purposes of claiming an estate tax charitable deduction, the amount of the deduction will be the property's fair market value in essentially all cases. The same holds true with regard to the gift tax charitable deduction. The only exceptions that will sometimes exist pertain to works of art (as opposed to the work's copyright), particularly any work with respect to which the donor while living gave to a charity an undivided fractional interest.

Conclusion

When a donor makes a charitable gift during life, one or more of the following may be relevant for income tax purposes:

- the concept of AGI and the use of a charitable deduction being limited in some way;
- whether the recipient is a public charity or a private, non-operating foundation;
- how long the donor has owned the asset in question;
- whether the asset has increased or decreased in value during that time; and
- in the case of tangible personal property, how the nature of the asset relates to the charity's mission.

When the same gift is made upon death, however, all of these distinctions can pretty much be ignored for estate tax purposes. Moreover, so long as the donor was a U.S. citizen or resident at the time of his or her death, the charitable recipient need not

even be a U.S. organization. Finally, because of its similarity to the estate tax, the federal gift tax ignores the distinctions in the case of its applicability to charitable gifts made during life.

Need help keeping track of the estate taxes upon death of a donor? *Bequest Manager* can project the remainder of that will go to your charity and estimate the bequest's future value.

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