

Making the Most of Your Client's Philanthropy Advanced Charitable Planning Techniques and Opportunities

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Key Points In All Circumstances

- **A non-charitable client shouldn't make charitable gifts.**
- **Appraised value is key for any transaction that is fun and interesting.**
- **Do not neglect the choice of the charitable recipient: public charity, donor advised fund, supporting organization, private operating foundation, private foundation. If all of your clients want to use only one of these, is your advice broad enough?**
- **Beware the Pre-Arranged Sale.**
- **Acknowledgment Letters. Just get them. No exceptions.**
- **The private foundation prohibited transactions are not audit risks you can afford to run.**
- **Form 8282.**
- **Avoid the section 338 rabbit hole**

Charitable Bailout of C Corporation Stock

- Donor has a \$25 million company with 10,000 shares of stock. Donor owns half the shares, and donor's children own the other half. Donor gives 100 shares of stock to a public charity. An appraiser values those shares at $\$2500 \times 100 = \$250,000 - 40\% \text{ discount} = \$150,000$.
- Donor receives an income tax deduction of \$150,000.
- Some time later, the company goes to the public charity and asks if it would like cash for the shares. The charity says sure, but we have to sell at appraised value. Suppose the shares have not changed in value. The charity is bought out for \$150,000.
- Suppose for ease of analysis the company had to borrow the \$150,000 to buy the shares.

- After the buy-back, the children own 5000 shares out of 9900. The company is worth $\$25,000,000 - \$150,000 = \$24,850,000$.
- The children owned 50% of a \$25,000,000 company. Now they own 50.5% of a \$24,850,000 company.
- The children have \$50,000 more than they did before donor made the gift.

- Does that worry you? Should it? Extrapolate.

Charitable Bailout With A Family Foundation

- The self-dealing rules prevent a company in most cases from buying its stock from a private foundation.
- Thus, for lifetime transfers a private foundation is a poor charitable donee.
- A testamentary transfer may be more promising because the shares can be bought back by the company from the donor's estate and the Probate Exception provides an exception to self-dealing.
- An interesting strategy is for a donor to create a trust during the donor's lifetime and to have that trust buy from the donor an option giving the trust the right to buy the donor's shares at the donor's death for a note (at fair interest). The donor's estate goes to a family foundation or to a charitable lead annuity trust. At the donor's death the trust exercises the option and the note goes either to the foundation or the CLAT.

Corporate Gift of Intellectual Property

- In Private Letter Ruling 200715015, a corporation formed a limited partnership and contributed to it exclusive ownership of certain trademarks and other intellectual property; the other partner was the owner of the corporation who contributed cash.
- The partnership granted the corporation a license to use that property in exchange for a royalty based on the corporation's net sales.
- The corporation then contributed the limited partnership units to a private foundation (created and managed by the owner).
- Because the limited partnership receives 95% or more of its gross income from passive sources (here, royalties), the units are not an excess business holding. Further, the foundation has no unrelated business income because royalties are exempt.

Gift of a Remainder Interest in a House or Farm

- What's a house or farm?
- One life or two
- Valuing the Remainder Interest

- But I have an *ancestral home*
- What if a donor gives a remainder interest to a public charity. After a period of time, the children, grandchildren, a trust for the children or grandchildren, offer to buy the remainder interest for fair market value from the charity.

- *Estate of Blackford v. Comm'r*, 77 T.C. 1246 (1981), acq. in result 1983-2 C.B. 1; Rev. Rul. 83-158, 1983-2 C.B. 159; PLR 8141037. See also Rev. Rul. 84-97, 1984-2 C.B. 196, in which a gift of a remainder interest in a farm was determined to qualify for an estate tax charitable deduction even though the applicable state mortmain statute required the charitable recipient to dispose of the farm within 10 years of acquisition.

Disclaimer to a Charitable Fund

- This is essentially the equivalent of a defined value clause. See, for instance, Estate of Helen Christiansen v. Commissioner, 130 T. C. No. 1 (2008) (reviewed), aff'd, 586 F.3d 1061 (8th Cir. 1061).
- Can also be used as an equalization device. Suppose all descendants have “enough” money. Some are charitable, others are not. Shares may be created for the descendants that are charged with their own share of federal and state transfer tax. A descendant who prefers charitable dollars to tax can disclaim. Other descendants need not. Each descendant can make a decision after the donor’s death based on the circumstances.
- Disclaimers to private foundations are problematic. See Private Letter Rulings 200616026, 9320008 and 9008011.
- Disclaimers to donor advised funds are fine because “advice” is not control. See Private Letter Rulings 200518012 and 9532027.

Charitable Gift Annuities

- A gift annuity is really a bequest substitute
- A deferred gift annuity may be the answer to the question “but what if I need the money?”
- In some instances, gift annuities may be useful to avoid the self-dealing rules applicable to charitable remainder trusts.

Rev. Rul. 2004-05

Gifts By Partnerships and LLCs

- Rev. Rul. 2004-05, 2004-3 IRB 295, provides that a trust which is a partner will benefit from a charitable contribution made by the partnership even if the trust itself has no charitable beneficiaries. The Ruling does not state how the trust came to be a partner.
- May a trust with no charitable beneficiaries become a partner in a partnership which allows charitable contributions without the consent of the trust partner?
- Who should be the general partner?
- Rev. Rul. 96-11, 1996-1 C.B. 140, holds that when a partnership makes a charitable contribution of property, the basis of each partner's interest in the partnership should be decreased, but not below zero, by the partner's share of the partnership's basis in the property contributed. Similarly, a partner's charitable deduction for the contribution of appreciated property by the partnership does not seem to be limited to her share of the partnership's basis in the assets. See Private Letter Ruling 8405084.
- Thus, contributions of appreciated property by partnerships preserve the tax benefit of receiving a deduction at fair market value for the contribution of appreciated property; the unrealized appreciation is not transferred to the partner's interest in the partnership.
- See also Private Letter Ruling 200208019, in which the IRS considered whether the members of a partnership were entitled to a charitable deduction on account of the partnership's grant of a conservation easement to a charitable organization. The IRS concluded that each partner was entitled to a charitable deduction equal to each partner's distributive share of the gift.

501(c)(4) - - 2015 Tax Act

- Under the Protecting Americans from Tax Hikes Act of 2015 (“PATH Act”), Code Section 2501(a) was amended to specifically exclude from federal gift tax “transfers of money or other property to an organization described in paragraph (4), (5), or (6) of section 501(c) and exempt from tax under section 501(a), for the use of such organization.”
- This exclusion from federal gift tax is applicable to lifetime gifts to 501(c)(4), (5), and (6) organizations.
- The PATH Act does not include a similar provision with respect to the federal estate tax. So this is a lifetime gift technique.
- As a general matter, donors should be wary of Code Section 2036 applying to excluded transfers under the PATH Act.
 - For example, a lifetime transfer by Donor to a 501(c)(4) organization that Donor controls, either alone or in conjunction with others, may be included in Donor’s estate for estate tax purposes.
 - The included amount would not be offset by a charitable deduction.

Using 501(c)(4) Organizations to Avoid Excess Business Holdings

- Scenario: Donor wants to contribute significant interests in a privately-owned corporation to her private foundation at death
- Problem: Section 4943 would preclude the private foundation from long-term ownership of more than 20% of the voting stock of corporation in combination with all disqualified persons.

Using 501(c)(4) Organizations to Avoid Self-Dealing

- Scenario: Donor's family wishes to engage in multiple transactions with family foundation
- Problem: Most transactions between disqualified persons and a related private foundation are prohibited under Code Section 4941
- If a 501(c)(4) organization is not a disqualified person – even if it is controlled by one or more disqualified persons -- it would be permissible for a private foundation and that 501(c)(4) organization to enter into transactions that ordinarily would be treated as self-dealing.

Trust Distributions Not Qualifying for Charitable Deduction

- Scenario: Trustee wants to make a distribution from a trust for charitable purposes and claim a deduction
- Problem: The trust has taxable income and DNI, but no assets traceable to gross income. Accordingly, a deduction under Code Section 642(c) is not permitted.
- Instead of distributing trust property to a charitable organization, the trustee could make a distribution of trust property to a 501(c)(4) organization to be used for charitable purposes
 - Trustee can claim a distribution deduction
 - No gift tax consequence

Other Trust Distribution Solutions

- 501(c)(4) solution requires a (c)(4)
- What about Rev Proc 2004-05? Form a partnership or LLC within the trust.
- The so-called BDOT solution. Beneficiary defective owned trust. You give charity the right to withdraw all (or however much you desire) of the trust's taxable income. Trust becomes taxable to charity under section 678.
- Elect ESBT status (if you have an S corporation). The 2017 tax act allows a charitable deduction to ESBTs for the first time.
- The IRS position is that if charity is not a permissible grantee you cannot add it later on. CCA 201651013.

<u>TYPE OF GIFT</u>	<u>DONOR BENEFITS</u>	<u>FAMILY BENEFITS</u>	<u>CHARITY BENEFITS</u>	<u>PREFERRED TYPE OF CHARITY</u>
Outright Gift of Undiscounted Assets	Full income tax deduction. No payments to donor.	-0-	Charity receives income and appreciation on the contributed assets from the date of gift.	For cash and marketable securities differences are minimal. For closely-held and real estate assets, private foundation gifts are less desirable.
Outright Gift of Discounted Assets followed by family purchase or redemption	Full income tax deduction. No payments to donor. Note that the restrictions on the gift could create a future interest thus eliminating the income tax deduction	Potential value received by the family through the purchase or redemption of assets that are discounted from pro rata value.	Charity receives income and appreciation on the contributed assets from the date of gift. However, enjoyment may be postponed if the assets are illiquid.	Donor advised fund or some supporting organizations are most desirable. Public charity is a good donee but may lack experience to handle the gift efficiently. Private foundation is undesirable because of self-dealing rules.
Defined value / charitable allocation clause transfer	Full income tax deduction. No payments to donor.	Potential for discounted assets to pass to the family transferring additional value.	Charity receives income and appreciation on the contributed assets from the date of gift. However, enjoyment may be post-poned if the assets are illiquid.	Donor advised fund or some supporting organizations are most desirable. Public charity is a good donee but may lack experience to handle the gift efficiently. Private foundation is undesirable because of self-dealing rules.
Bequest	No income tax deduction. No payments to donor.	-0-	Assets available at an undetermined future date.	No substantial differences. Bequests to a private foundation may be “bought out” by the family using the Probate Exception.
Disclaimer to a Charitable Fund	No income tax deduction. No payments to donor.	Potential for discounted assets to pass to the family transferring additional value.	Assets available at an undetermined future date.	Donor advised fund or some supporting organizations are most desirable. Public charity is a good transferee but may lack experience to handle the gift efficiently. Private foundation is undesirable because of self-dealing rules regardless of the probate exception.

<u>TYPE OF GIFT</u>	<u>DONOR BENEFITS</u>	<u>FAMILY BENEFITS</u>	<u>CHARITY BENEFITS</u>	<u>PREFERRED TYPE OF CHARITY</u>
Gift Annuity	Partial income tax deduction. Annuity payments to donor.	-0-	Assets available immediately, subject to an obligation to make annuity payments.	Public charity is almost always the best choice.
Charitable Remainder Trust	Partial income tax deduction. Annuity or unitrust payments to donor.	-0-	Assets available in the future, date may or may be fixed. Asset may be monetized through a fair market value sale.	The income tax deduction for gifts to private foundations is limited and monetizing the interest of a private foundation may be difficult.
Remainder interest in house or farm	Partial income tax deduction. Donor may use the house or farm for life.	If remainder interest is purchased by the family, potential for value to transfer depending on the appreciation rate of the asset and the length of the donor's life.	Assets available in the future at a date that is not fixed. Asset may be monetized through a fair market value sale.	Private foundations are undesirable recipients.
Charitable Lead Trust - - Constant Annuity	Typically no income tax deduction but income is removed from the donor's taxable income base. No payments to donor.	Assets available in the future, date may or may not be fixed.	Annuity or unitrust payments to charity.	Any charitable donee. Private foundations do not have to include the assets of the lead trust when calculating the annual 5% distribution.
Charitable Lead Trust - - Increasing Annuity or Shark-Fin CLAT	Typically no income tax deduction but income is removed from the donor's taxable income base. No payments to donor.	Assets available in the future, date likely to be fixed at the end of a specified term.	Annuity payment to charity largely deferred until the end, or close to the end, of the trust term. Minimal payments until then.	Private foundations less desirable because the charitable donee must be free to challenge the investment of trust assets during the term, and to ensure that all trustee actions are independent.