

Charitable Intent



PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

CHARITY BENEFITS TWICE FROM THIS TRUST

The rules governing charitable remainder unitrusts provide that they must pay a unitrust amount at least annually to one or more persons, at least one of which is not a charity [Code §664(d)(2)]. A donor proposed to fund a charitable remainder unitrust from which she would retain 25% of the annual payment for her life and then her husband's life. A special trustee could choose to have the remaining 75% paid to the donor during her life, her husband after her death, or any charity. Neither the donor, her husband nor any person related or subordinate to them could act as special trustee.

The IRS ruled that a provision giving an independent special trustee the power to allocate a portion of the unitrust amount among charitable and noncharitable beneficiaries on an annual basis is not inconsistent with the rules governing charitable remainder trusts. The trust is therefore not precluded from qualifying as a charitable remainder trust under Code §664(d)(2).

Letter Ruling 200832017

PUTTING FAMILY FIRST NOT CHARITABLE

A nonprofit organization that conducts genealogical research related to a single family is not qualified for tax-exempt status under Code §501(c)(3), the IRS ruled. The group is organized exclusively for charitable, educational and other exempt purposes, but its stated purposes are the preservation and promotion of the history, traditions and heritage of a particular family. Associate memberships are open to anyone, but only those who can show they are direct lineal descendants of an individual with a given surname may vote or hold office. The IRS noted that while some of their research material is useful to non-family members, it is primarily focused on the single family line.

Reg. §1.501(c)(3)-1(d)(1)(iii)(ex. 1) gives the example of an educational organization whose purpose is to study history and immigration. However, because a major purpose of the group's research is to

identify and locate living descendants of a particular family, the group's educational activities "primarily serve the private interests of members of a single family rather than a public interest." It is not operated exclusively for exempt purposes and is not eligible for Code §501(c)(3) status.

The IRS said that, in a similar manner, this group conducts research primarily for the benefit of one particular family. While some of the activities are educational and research is performed for individuals outside the family, that is an insubstantial part of the activities.

Letter Ruling 200841039

TESTIMONY, DOCUMENTATION SUFFICIENT FOR TAX COURT

Donald and Penny Nicholas had AGI of slightly less than \$90,000 in 2005, but claimed a charitable contribution of more than \$43,000, including \$6,000 of carryover from the previous year. Their tax preparer reported the full amount as cash gifts, although about \$4,900 was noncash contributions of books, CDs and furniture.

When the IRS began examining their 2005 return, the couple realized the noncash gifts had been reported incorrectly. They filed a timely amended return including a Form 8283, Noncash Charitable Contributions. The IRS allowed the \$32,875 cash contribution, for which the Nicholases had substantiation, but disallowed the entire deduction for the noncash gifts.

Penny maintained a list regarding the types of assets, names of charitable recipients, costs and estimated value of the noncash contributions. In nearly every instance, she had a receipt and/or letter from the charitable recipient. Most of the gifts were for less than \$500. The Tax Court noted that although she did not have receipts to substantiate the original costs, she had been the purchaser and recollected the amounts paid. Even more important, said the court, was that as a frequent shopper of garage sales and flea markets, she "had a keen sense of the value of her contributed items."

The court said that although the couple's evidence for their noncash gifts was "less precise" than that for their cash contributions, it was persuaded that the assets were contributed and that the values were "appropriately derived." The court noted the couple's extreme generosity, as reflected by their cash contributions of approximately half their income, and added that the cash gifts represented nearly 90% of their total gifts for the year. The tax deficiency attributable to the disallowance of the noncash gifts was only \$712, said the court, but the donors pursued the case "as a matter of principle." The court accepted her testimony and documentation and ruled the couple was entitled to the \$4,900 deduction.

Nicholas v. Commissioner, T.C. Summ. Op. 2008-155

N O CHARITABLE DEDUCTION WITHOUT A DISPUTE

A decedent designated a testamentary trust as the death beneficiary of his IRA. The IRA was the trust's only asset. The trust provided that a specified percentage of the trust property was to be distributed annually to the decedent's children and to charities. The trust had no termination date and contained no provisions for payment of a child's share when the child dies. The trust was reformed to ensure that it would meet the definition of a designated beneficiary trust under Code §401(a)(9). As reformed, the charities received an outright distribution of a

portion of the trust, equal to their interest under the original trust. The balance of the trust was to be held in separate shares for the children, with outright distributions at a specified age.

Reg. §1.642(c)-1(a)(1) provides that a trust is allowed a deduction for any part of the gross income which, pursuant to the governing instrument, is paid during the taxable year for charitable purposes. In *Emanuelson v. U.S.* [159 F.Supp. 34 (D.C. Conn. 1958)], a written compromise was reached to resolve the differences between two conflicting wills. The court said that outright payments made to charities under the compromise were made pursuant to the will. The IRS later issued Rev. Rul. 59-15 (1959-1 C.B. 164), citing *Emanuelson*, which held that settlement agreements arising from will contests qualify as governing instruments.

The IRS noted that the purpose of the reformation was not to resolve a conflict, but rather to obtain tax benefits available if the trust qualified as a designated beneficiary under Code §401(a)(9). Neither Rev. Rul. 59-15 nor *Emanuelson* holds that a modification not resulting from a conflict will be construed as the governing instrument. Therefore, ruled the IRS, the accelerated payments to the charities are not considered to be made pursuant to the governing instrument and the trust is not entitled to a deduction under Code §642(c).

Letter Ruling 200848020

WHY QCDs STILL MAKE SENSE

Congress has suspended, for 2009 only, required minimum distributions from IRAs and 401(k) plans by those age 70½ and older, as part of the Worker, Retiree and Employer Recovery Act of 2008. The concern was that owners would be taking RMDs, based on account values on December 31, 2007, from accounts that had declined dramatically in value during 2008. Because RMDs are not required this year, qualified charitable distributions (QCDs) from IRAs directly to charities will not be "saving" the donors from tax that they would otherwise owe. But gifts from IRAs may still make sense, particularly for taxpayers who take the standard deduction and therefore receive no tax benefit from their generosity. A gift from an IRA is made with funds that have never – and will never – be subject to tax at ordinary income rates. Donors age 70½ and older may give up to \$100,000 to charity by December 31, without recognizing income from the distribution. For clients with large IRAs and those with potential estate tax concerns, reducing the value of the account through QCDs can result in lower income and estate taxes in future years. If you'd like to know more about how a QCD can help a client and The Salvation Army, please feel free to call our office.