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THE SALVATION ARMY

Charitable Intent

PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

DOING THE MOST GOOD℠

MINOR DIFFERENCE DOESN'T CREATE AMBIGUITY

Frederick Scale left 10% of the residue of his estate to "The Audubon Society of New York State." Both the Audubon Society of New York State, Inc. and the national organization – National Audubon Society, Inc. – claimed to be the intended beneficiary. The Surrogate's Court allowed the introduction of an affidavit to resolve the ambiguity. The attorney who drafted the will indicated that, although Scale said he intended to benefit the state organization, the attorney thought he actually meant the national society. The court ruled that the national organization should receive the bequest.

The Appellate Division of the Supreme Court of New York agreed with the state Audubon Society that the will was unambiguous on its face and therefore the court erred in allowing extrinsic evidence of the testator's intent. The failure to include "Inc." in the will did not render the bequest ambiguous, said the court.

The national organization argued that the phrase "Audubon Society" is used by many charities, creating a latent ambiguity. The court, however, said that the use of the phrase and allegations of public confusion did not "give rise to a latent ambiguity" that would justify the admission of extrinsic evidence. The Surrogate's Court erred when it relied on the attorney's affidavit, in which he speculated that Scale meant the national organization when he unequivocally stated that he wished to benefit the state organization.

***In the Matter of Scale*, 2007 NY Slip Op 01660**

CHARITABLE TRANSFERS CAME FROM EXERCISE OF POWER OF APPOINTMENT, NOT TRUST

Lucien Brownstone created a testamentary trust for his wife, Ethel, giving her the power to distribute the remaining principal at her death. If Ethel did not exercise the power, trust assets would pass to a foundation. At her death, Ethel directed that the residue of the trust be divided among eight charities. The trust transferred $1 million to Ethel's estate for the charitable distributions. The trust paid income tax, but later filed an amended return seeking a refund. The trustee claimed that the distributions pursuant to Ethel's exercise of the power of appointment were charitable distributions under Code §642(c)(1). The IRS denied the refund. The district court granted the IRS's motion for a summary judgment, noting that the distribution was not made "pursuant to" Lucien's will.

Under Code §642(c)(1), a deduction is allowed for any gross income that, pursuant to the terms of the governing instrument, is paid for a charitable purpose. The trustee argued that Ethel's power of appointment, coupled with Lucien's will, constituted the governing instrument. However, both the district court and the U.S. Court of Appeals (2d Cir.) pointed out that the language of Code §642(c)(1) is singular. The governing instrument was Lucien's will, said the court, noting that Ethel could have distributed the entire principal to private individuals. Lucien's will did not compel Ethel to give any funds to charity, so the transfers were not "pursuant to" Lucien's will and did not qualify for a charitable deduction.

***Brownstone v. U.S.*, 2006-2 USTC ¶50,528**

INCOME BENEFICIARY NOT ENTITLED TO DEDUCT "TRUST'S" GIFT

Thomas Goldsby was the income beneficiary and trustee of a trust created by his father. His children were the remainder beneficiaries. For many years, Goldsby chose not to take the annual income distributions, instead allowing the funds to accumulate in the trust. By 2000, the undistributed net income was about $2.2 million.

In 2000, the trust conveyed conservation easements over several parcels of land to the Mississippi Land Trust. An appraisal put the value of the easements at $5,640,000, which the trust treated as a pass-through to Goldsby on the Schedule K-1. Goldsby claimed the charitable deduction on his personal return in 2000, with carryovers to later years.

The IRS challenged both the value of the

deduction and Goldsby's right to claim it. Goldsby argued that, as the owner of a portion of the trust, he could claim the deduction. The Tax Court noted that, while he was the owner of the income portion of the trust, he was not the owner of the corpus. A trust beneficiary may take a personal deduction for gifts to charity made from that portion of the trust that he or she owns [Reg. §1.671-2(c)].

The court ruled that Goldsby did not prove that the conservation easements came from the income portion of the trust. The fact that he left undistributed income in the trust does not make him the owner of a portion of the corpus, said the court, noting that he had not relinquished his right to withdraw the income at any time. The income was not held subject to the trust agreement and therefore was not part of the corpus. Furthermore, said the court, Goldsby did not explain how the $2.2 million in undistributed income related to the $5.6 million easement contribution. Because he was not entitled to the deduction, the court did not address the valuation issue.

***Goldsby v. Comm'r.*, T.C. Memo 2006-274**

CHARITABLE DISTRIBUTIONS DON'T CHANGE TRUST

The terms of a complex trust allowed distributions of part or all of the trust's income to charities selected by the trustees. The IRS had earlier ruled that income paid to charity pursuant to the trust's language would entitle the trust to a deduction under Code §642(c). The IRS was then asked to rule on whether discretionary distributions made in the exercise of the trustees' power would cause the trust to be characterized as a split-interest trust.

Under Code §4947(a)(2), certain private foundation rules are applicable to split-interest trusts in which not all of the interests are devoted to charitable purposes.

The IRS noted that the trust is not exempt from tax under Code §501(a) and a deduction has not been allowed under Code §§170, 545(b)(2), 642(c), 2055, 2106(a)(2) or 2422. The trust has not permanently set aside any amounts for charitable purposes, and any distributions to charity are free of trust. The trustees' exercise of discretionary power to make distributions of income therefore will not result in the trust coming within the provisions of Code §4947(a)(2).

Letter Ruling 200714025

ADAPTING TO THE NEW RULES

The Pension Protection Act tightened the requirements on substantiation of cash gifts to charity. Previously, only gifts in excess of $250 required written acknowledgment from the charity. For tax years beginning after August 17, 2006, deductions for gifts of any size must be substantiated by a bank record or a written communication from the charity showing the name of the organization, the date of the gift and the amount [Code §170(f)(17)].

Prior to the changes in the PPA, gifts of less than $250 made through payroll deductions were not required to be substantiated. Now, donors are entitled to the deduction if they have a pay stub, W-2 or other employer-furnished document setting forth the amount withheld, along with a pledge card prepared by or at the direction of the charity. These will be considered "written communication from the donee organization," said the IRS.

NOTICE 2006-110

CHARITABLE GIFT ANNUITIES – THE ALL-PURPOSE GIFT

Donors at all levels of income and net-worth have discovered how charitable gift annuities can allow them to make gifts while providing lifetime payments for themselves or others. Most gift annuities are funded with cash or appreciated securities, which can minimize capital gains taxes and create large deductions. Gift annuities also enable donors to address a wide range of estate planning concerns. For example: Retirement plan assets can be left to charity at death, contingent on the issuance of a gift annuity to a loved one, with no immediate tax on the income in respect of a decedent; deferred gift annuities can be used to establish "retirement plans" for children; or gift annuities can be arranged when a client sells a home after retirement, allowing the donor to receive annuity payments during life after moving to a retirement community. Because gift annuities can be arranged in smaller amounts than required with some other charitable techniques, they appeal to clients who want to help but don't feel they can part with assets. We would be happy to discuss how a gift annuity might address your clients' particular charitable objectives.