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Charitable Contributions of Tangible Personal Property:

An Overview of the Rules

Charitable contributions of TPP can provide clients with significant income tax benefits as well as immense personal satisfaction.

At this time of year, many lawyers have the opportunity to counsel their clients concerning the advisability of making gifts to charitable organizations. One aspect of charitable giving often overlooked is charitable gifts of tangible personal property (TPP) such as works of art, furniture, books, collectibles, jewelry and cars. Perhaps this is because of the complexity of the tax rules involved and the unfamiliarity of many lawyers with these rules. This article provides a general overview of the principle rules relevant to the tax treatment of lifetime charitable gifts of TPP, which may serve as a useful checklist for lawyers advising their clients on this subject. (Detailed rules may be found in Section 170 of the Internal Revenue Code and the regulations thereunder.)

VALUE OF CONTRIBUTION

Lifetime transfers of TPP to charitable organizations allow a donor to receive a federal income tax deduction for part or all of the fair market value (FMV) — the price at which property would change hands between a willing buyer and seller — of the property contributed. The first step in determining the deduction associated with a lifetime transfer of TPP to a charitable organization is to determine the value of the contribution to which the deduction will apply.

Contributions of Property that has Decreased in Value

When a taxpayer makes a contribution of TPP with a FMV that is less than the amount the taxpayer paid for the property (the taxpayer's "basis") such as clothing and cars, the deduction is limited to the actual FMV of the property at the time of the contribution.

Contributions of Appreciated Property

For contributions of property for which the FMV of the property exceeds the taxpayer's basis, the nature of the contributed property is significant in calculating the charitable deduction.

Gifts of Ordinary Income Property

Ordinary income property is property that, if sold at its FMV on the date of contribution, would have resulted in ordinary income or in a short-term capital gain. Examples include a work of art created by the donor, property received as a gift from the creator, property held as inventory by a dealer, and property owned for less than one year before being contributed. For purposes of calculating the income tax deduction for a contribution of such property to a charitable organization, the value of the contribution is generally limited to the taxpayer's basis in the property.

Gifts of Capital Gain Property

Generally, the value of a taxpayer's contribution of "capital gain property" to a charitable organization will be the full FMV of such property at the time of contribution. Capital gain property includes any property that, if sold at its FMV at the time of contribution, would have resulted in a long-term capital gain. In certain situations, the value of a taxpayer's contribution of capital gain property to a charitable organization is limited to the taxpayer's basis in the property. The value of a taxpayer's contribution of capital gain property is limited to the taxpayer's basis in the property if the property is contributed to a private foundation other than a private operating foundation. The value of a taxpayer's contribution of capital gain property is also limited to his or her basis in the property if the property does not satisfy the related use rule (discussed below) or if, pursuant to

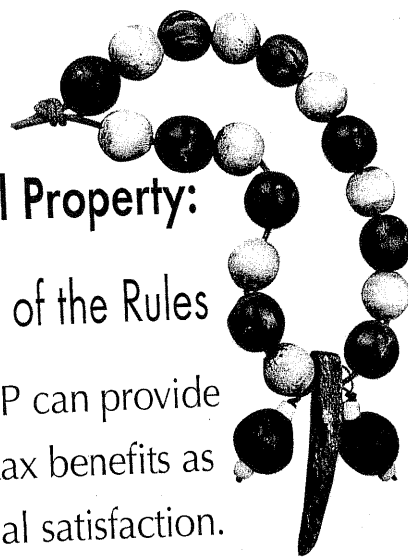
such rule, the taxpayer elects to increase the 30 percent limitation to 50 percent of his or her contribution base. (A taxpayer's contribution base for a year is the taxpayer's adjusted gross income without regard to the net operating loss carryback to the year.)

PERCENTAGE LIMITATIONS

The extent to which the taxpayer may deduct such contributions of TPP is ultimately determined by the application of the appropriate percentage limitations to the taxpayer's contribution base.

Generally, a taxpayer's charitable deduction for contributions of ordinary income property to a public charity (i.e., churches, schools, museums) is limited to 50 percent of the taxpayer's contribution base. For contributions to a private charity, the charitable deduction is limited to the lesser of 30 percent of the taxpayer's contribution base; or the excess of 50 percent of the taxpayer's contribution base for the taxable year over the amount of charitable contributions allowable to public charities.

The applicable percentage limitation for contributions of capital gain property to a public charity is dependent on satisfaction of the related use rule, which requires that the use of the TPP by the charitable organization be related to the purpose or function of the organization upon which the charitable organization's tax exemption is based. The related use rule is satisfied if the taxpayer establishes that the property is not in



fact put to an unrelated use by the charitable organization or if it is reasonable for the taxpayer to anticipate that the property will not be put to an unrelated use by the charity. If the use of a donated item of TPP is not related to the charitable organization's exempt purpose, the value of a taxpayer's contribution is limited to the taxpayer's basis in the property, and the taxpayer's charitable deduction is limited to 50 percent of the taxpayer's contribution base. However, if the contribution satisfies the related use rule, the taxpayer's charitable deduction is limited to 30 percent of the taxpayer's contribution base (unless the taxpayer elects to increase the percentage to 50 percent of the contribution base, in which case the value of the contribution would be limited to the taxpayer's basis in the property).

The percentage limitation to be applied to contributions of capital gain property to a private charity is the lesser of 20 percent of the taxpayer's contribution base; or the excess of 30 percent of the taxpayer's contribution base over the amount of the taxpayer's charitable contributions allowable for gifts to public charities.

The amount of any contribution that exceeds the applicable percentage limitation may be carried forward for five years, retaining its character as ordinary income property or capital gain property.

APPRAISAL REQUIREMENTS FOR CONTRIBUTIONS IN EXCESS OF \$5,000

To substantiate a contribution of TPP in excess of \$5,000, the taxpayer must obtain a qualified appraisal for the TPP contributed, attach an appraisal summary to the tax return and maintain records containing specific information about the contribution. If the taxpayer does not conform strictly to the substantiation requirements, no deduction is allowed for a contribution of TPP.

The appraisal must be signed and dated by a qualified appraiser and must include, among other things, a detailed description of the property, the identification and qualifications of the appraiser, the date on which the property was valued, the appraised FMV of the property and the method of valuation used to determine the FMV. The appraisal must be received by the donor before the due date (including extensions) of the taxpayer's return. The entire charitable deduction is lost if the appraisal is not obtained on a timely basis.

FRACTIONAL INTEREST GIFTS TO CHARITABLE ORGANIZATIONS

The gift of a fractional interest in tangible personal property to a charitable organization provides an opportunity for the taxpayer to receive an immediate charitable income tax deduction while still retaining possession of the property on a part time basis. The transfer of an undivided fractional interest in an item of tangible personal property is not a transfer of a future interest that would not be deductible under Section 170(a)(3) or Section 170(f) of the Internal Revenue Code. Therefore, a

taxpayer can transfer an undivided fractional interest in an item of tangible personal property to a charitable organization and receive an immediate charitable deduction for the value of the donated fractional interest. For example, if a taxpayer transfers an undivided one-fourth interest in a painting to an art museum by a deed of gift, the taxpayer would be entitled to the possession of the painting for nine months of the year, the museum would be entitled to possession of the painting for three months of the year, and the taxpayer would be entitled to a charitable deduction for one-fourth of the fair market value of the painting on the date of the gift, subject to the applicable percentage limitations.

Charitable contributions of TPP can provide clients with significant income tax benefits as well as immense personal satisfaction. Attorneys should remember this effective planning tool when advising their clients regarding charitable giving. ■

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*Isabella Brant, c. 1620-25.
Peter Paul Rubens (Flemish,
1577-1640). Oil on wood,
53 x 46 cm. Mr. and Mrs.
William H. Marlatt 1947.207*

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