
NEW HOPE CHRISTIAN COMMUNITY FOUNDATION

Spring
2005

A newsletter about charitable gift planning and
exempt organizations for professional advisors and
local Christian foundations.

INDEX

Tsunami Relief	Page 1
Gift Annuities with Flexible Starting Dates	Page 1
IRS Issues Indexed Tax Adjustments for 2005	Pp 1-2
Correcting Drafting Errors in Charitable Remainder Trusts	Page 2
Guidelines for Tax Opinion Communications	Page 2
Limitation on Charitable Deduction for Vehicles and Intellectual Property Donations	Page 2
When is a Church a Church?	Page 3
New Form 1023 and Instructions	Page 3
Allocating Income in Respect of a Decedent (IRD) to Charity	Page 4
e-Filing IRS Form 8283	Page 4

Editor
Dennis F. Keller, J.D

©Dennis F. Keller 2005

TSUNAMI RELIEF

Congress has authorized taxpayers to deduct contributions made in January, 2005 to U.S. charitable organizations for tsunami relief on their 2004 tax returns. The U.S. charitable organization must have full control and discretion over the use of the funds contributed to assist individuals in foreign countries. Contributions to specific individuals are not deductible. Gifts to such individuals would not be subject to federal income tax, but the donor would have to use some or all of his/her gift tax annual exclusion. If the gift exceeded the annual exclusion, the donor would have to use some of his/her one million dollar gift tax exemption. For more information, see IRS pub. 3833, Disaster Relief. You can find this publication at the IRS's website: www.irs.gov .

GIFT ANNUITIES WITH FLEXIBLE STARTING DATES

Typically, a charitable gift annuity (CGA) has a specified starting date. However, sometimes the donor wants the annuity to start at a later date, perhaps to provide retirement income. The IRS has recently issued a Private Letter Ruling approving such an arrangement. In this case, the donor sought to have the annuity payments begin during the period of eight (8) years from the time the donor reached a certain age. When the donor decides when the payments are to begin, the annuity payments will be determined based on the donor's age at the time the payments begin. The agreement with the charities set forth various commencement dates with corresponding rates payable for the respective starting dates. Because the starting date is not fixed, the exact value is not determinable. In this case, the IRS proved giving the highest possible value to the annuity portion based on the mortality tables and interest rates specified in Internal Revenue Code (IRC) Sec. 7520. This results in the charitable deduction being the lowest possible amount. See letter ruling 200449033. The IRS has made similar rulings in the past. See Private Letter Rulings (PLR) 9017071 and 9743054.

IRS ISSUES INDEXED TAX ADJUSTMENTS FOR 2005

The IRS has issued indexed tax adjustments relating to charitable deductions and charitable gift premiums as well as various other matters. For 2005, tax payers are required to reduce their itemized deductions, including charitable deductions (but not medical expenses, casualty and theft losses, and investment interest) by an amount that equals three (3%) percent of their adjusted gross income over \$145,950.00 for couples, and over \$72,975.00 if married filing separately. Also, donors are not required to reduce their charitable deductions when they receive items of "insubstantial value". If what the donor receives has a fair market value of \$83.00 for two (2%) percent of the payment, whichever is less, or the donor gives the charity at least \$41.50 and receives a low cost or token item that costs the charity no more than \$8.30. These are safe harbors. However, the IRS acknowledges that these are guidelines only and the facts and circumstances of

individual cases may permit a larger benefit to the donor. For example, a donor might make a gift of three million dollars and receive in return a benefit with \$250.00. This might still be an “insubstantial benefit” even though not within the guidelines. You should also note that the estate tax exemption is one and one-half million dollars for 2005 (increasing to two million dollars in 2006), and the gift tax exemption remains at one million dollars in 2005 and future years. The annual gift tax exclusion remains at eleven thousand dollars per person per year in 2005, which can be doubled by gift splitting with a spouse.

CORRECTING DRAFTING ERRORS IN CHARITABLE REMAINDER TRUSTS

Charitable Remainder Trusts (CRT) are complex and mistakes are made in drafting the documents. The IRS calls these “scrivener’s errors”. The IRS has been very generous in allowing reformation or correction of scrivener’s errors. Often this is done through reformation in a state court. Each case seems to be decided on its own merits. There have been several Private Letter Rulings in this regard. The following are some of them: PLRs 200447033, 200441019, 200338006, 200251010, 200218008, 9804036, and 9822041. A CRT can also be reformed by the trustee amending it or a court construing it. For the rules governing amendment, reformation and construction, including a 90 day deadline in certain circumstances, see IRC Sec. 2055(e)(3). A CRT can be fixed by disclaimer or rescission as well. Of course, your first line of defense is a well drafted trust. Use a checklist. Consider including a trustee’s right to amend for the purpose of complying with IRC Sec. 664. You can also give the income beneficiary, the grantor or the trustee the right to change the charitable beneficiary. See Rev. Rul. 76-7, 1976-1 CB 179; Rev. Rul. 76-8, 1976-1 CB 179; and Rev. Rul. 76-371, 1976-2 CB 179.

GUIDELINES FOR TAX OPINION COMMUNICATIONS

The IRS has issued new Circular 230, which establishes so-called best practices for practitioners rendering “covered opinions” which is a term defined in the Circular. The term “covered opinions” is broadly defined. Many commentators are concerned that this standard can be applied to communications between tax advisors and estate planning clients. You can obtain a copy of Circular 230 and download it from the IRS website at www.irs.gov.

LIMITATION ON CHARITABLE DEDUCTION FOR VEHICLE AND INTELLECTUAL PROPERTY DONATIONS

The IRS has issued new rules concerning the deductibility of vehicle and intellectual property donations. The rules for vehicles are effective for contributions made after December 31, 2004. The rules also apply to contributions of boats and planes. If the claimed value of the donated vehicle, boat or plane exceeds \$500.00 and the item is sold by the charitable organization, the taxpayer is limited to the gross proceeds from the sale.

If the charity significantly uses or materially improves the vehicles, the charity must certify this intended use and its duration, and provide an acknowledgement to the donor within thirty (30) days of the contribution. If the charity significantly uses or materially improves the vehicle, generally, the donor may deduct the vehicle's market value.

The donor of patents, copyrights and other intellectual property can deduct only the lesser of the tax basis in the property or its fair market value. The donor can then take additional annual deductions based on a percentage of the income received or accrued by the charity from the property, but only after the charity has received or accrued such income in an amount exceeding the donor's deduction. Then the additional deduction declines on a sliding scale from 100% of the income allocable to the property itself the first 2 years and declining 10% at year after that. The donor has to tell the charity up front of his/her intention to take the additional deductions, and the charity must report such income to both the IRS and the donor annually. The rules for intellectual property are retroactively effective to June 4, 2004.

For more information, see IRS Pubs. 526 and 561.

WHEN IS A CHURCH A CHURCH?

The IRS has issued an interesting ruling that sets forth the basis for determining whether a church is a church for income tax purposes. Included in the ruling is a list of fourteen points used by the IRS in distinguishing a "church" from other religious organizations. For more information, see Private Letter Ruling 200502044 and American Guidance Foundation, Inc. v. United States, 490 F. Supp. 304 (1980).

NEW FORM 1023 AND INSTRUCTIONS

The IRS has revised Form 1023, the Application for Recognition of Exemption under IRC Sec. 501(c)(3). Many of the changes reflect the changing attitude at the IRS and in Congress that are reflected in proposals coming from the Senate Finance Committee and the Joint Committee on Taxation. There are many and detailed questions concerning governance and compensation issues. The new Form 1023 and instructions can be found at the IRS website, www.irs.gov. The proposals from the Senate Finance Committee and the Joint Committee on Taxation include requiring a five-year review of exempt status of public charities and private foundations; penalties for involvement of tax-exempt entities in tax shelter transactions; further reform of intermediate sanctions to curb abuses by insiders and managers of public charities involving compensation packages, loans, sales to insiders, etc.; increasing the amount of excise taxes imposed on public charities, social welfare organizations, and private foundations; limitations on charitable deduction for contributions of clothing and household items; reformation of rules for charitable contributions of all kinds of property; requiring public disclosure of Form 990-T, the annual return for unrelated business income tax; and reformation of rules relating to donor advised funds, including requiring minimum annual payouts and prohibiting

distributions from donor advised funds to individuals. There is a Senate Finance Committee white paper containing the proposals, which can be found at www.house.gov/jct/s/2/05.pdf , and an explanation can be found at www.treas.gov/offices/tax-policy/library/bluebk05.pdf .

ALLOCATING INCOME IN RESPECT OF A DECEDENT (IRD) TO CHARITY

The IRS has recently ruled that a non-pro rata allocation of IRD, by assignment of IRAs and annuity contracts, from an estate to a public charity in satisfaction of the charity's share of the residue will not cause the estate or beneficiaries to incur taxable income or cause the estate to include any amount in its distributable net income. See PLR 200452004. This should remind us to take IRD into consideration when drafting. Usually, you want to purposefully transfer IRD by beneficiary designation so as to avoid acceleration of the income under IRC Sec. 691(a)(2). Consider allowing the personal representative to allocate IRD to fractional charitable bequests as a safety measure.

e-FILING IRS FORM 8283

The IRS has announced that it can only accept page one (1) of Form 8283, Non-Cash Charitable Contributions, by eFile until the new form for 2004 comes out in June or July. Returns e-Filed with page two (2) will be rejected.

NOTE THAT A PRIVATE LETTER RULING IS NOT A PRECEDENT AND CAN ONLY BE RELIED ON BY THE TAXPAYER TO WHOM IT IS ISSUED. THEY ARE HOWEVER AN INDICATION OF WHAT THE IRS IS THINKING.
If it is important enough to your client (and when isn't it) obtain your own ruling.

To find the cases, statutes and rules cited in this newsletter, try the following free websites:

www.findlaw.com

www.firstgov.gov

www.access.gpo.gov

www.irs.gov

www.law.cornell.edu

Tell the people that every man is to ask his neighbor and every woman is to ask her neighbor for objects of silver and gold. Exodus 11: 2.