NATIONAL CAPITAL GIFT PLANNING COUNCIL

15TH ANNUAL PLANNED GIVING DAYS
WASHINGTON, D.C.

ALPHABET SOUP
CHARITABLE USES OF FLPS
LLCs AND S CORPORATIONS

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Key Bridge Marriott
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I. Gifts of Closely Held Corporate Stock

1. Background on Corporate Income Taxation.

A. Generally, corporate income is subject to double taxation. First, the corporation pays corporate income tax on its net income. Then, the corporate shareholders pay income tax on receipt of dividends or on distributions of corporate assets when the corporation terminates. There is some relief from double taxation for S corporations, as discussed below.

B. Example: Jane Donor created a corporation some years ago and made a capital contribution of $10,000.00. The closely held corporation has assets worth $200,000 with a tax basis of only $40,000. Jane believes that her stock is worth $200,000 - - the value of the corporate assets. However, if the corporation sold those assets and liquidated, the IRS would collect approximately $81,520 of income tax and Jane would be left approximately $108,500.

Corporation:	Sells assets worth	$200,000
	Tax basis	40,000
	Taxable gain	$160,000
	Corporate tax (assuming 34% tax bracket)	54,400
	Proceeds left for shareholder (Sales proceeds of $200,000 less $54,400 tax) =	$145,600
Shareholder:	Liquidating distribution of net proceeds	$145,600
	Less: Jane's cost basis	10,000
	Long-term capital gain	$135,600
	Capital gains tax (20%)	27,120
	Net proceeds to Jane	$108,480

C. The result would be the same if the corporation merely distributed its assets to the shareholder because the law requires the corporation to pay income tax as if it had sold its assets and the shareholder is treated as if she had sold her stock.

The tax burden would be even worse if the distribution of assets were treated as a dividend to the shareholder because then the corporation still pays income tax as if it had sold the assets but the shareholder pays ordinary income tax on the value of the assets received rather than the more beneficial long-term capital gain rate.

D. Clear Conclusion: Keep appreciated assets, such as real estate, out of a C corporation. The problem is that the gift planner must deal with that fact because the shareholder/donor has already placed assets inside the corporation.

E. The corporation itself can contribute assets to a charity or a charitable remainder trust and avoid the tax on the assets' growth if sold by the charity or the trust but, if a trust is established, the income stream would be paid to the corporation, taxed to the corporation at its rates and then, when distributed to the shareholders, would generate regular income tax as a dividend.

2. Gifts of Closely Held Stock.

A. Gift of appreciated publicly traded stock to charity - - whether a public charity or a private foundation - - will still generate a double tax benefit: A charitable contribution deduction based on the fair market value of the stock with no realization of capital gain income.

B. However, the benefits obtained on a gift of closely held corporate stock will depend upon the charitable donee:

(1) If the gift is to a public charity, the deduction is still at fair market value with no realization of capital gain income;

(2) If the gift is to a private foundation, the deduction is for cost basis only;

(3) There are also higher ceiling limitations for gifts to a public charity than to a private foundation, as follows:

Kind of Charity	Cash or Ord. Inc. Prop.	Long Term Cap. Gain Prop.
Public Charity	50% of AGI	30% of AGI
Private Non-Operating Foundation	30% of AGI	20% of AGI
Private Operating Foundation	50% of AGI	30% of AGI

A five year carryover for any "excess" contribution is allowed in each case.

C. Qualified appraisal required. See below for discussion of valuation and substantiation rules.

3. Life Income Arrangements.

A. If publicly traded securities are transferred to, for example, a charitable remainder trust, the results are clear and there are ordinarily no problems with a deduction for the remainder value calculated on the full fair market with no imputing of the gain to the donor and generating an income stream which will generally increase the donor's income.

B. Using closely held C corporation stock. Example: John and Jane Donor, both age 65, are about to sell their corporate business for $10,000,000 that they started many years ago and which has basically a zero cost basis. Before the sale is a binding obligation, they transfer $1,000,000 of that stock to a charitable remainder unitrust at 7% retaining the income stream jointly and for the survivor of them. The below chart shows that, by avoiding capital gains tax, they receive an income stream of $70,000 rather than $56,000, an increase of 25%. And, they have generated an income tax charitable contribution deduction of approximately 25% of the value of their gift or $250,000 which is money in their pockets and which can be used for themselves or their heirs.

	Sell the Stock Personally	Transfer Stock to CRUT Which Sells
Sales Price	$1,000,000	$1,000,000
Cost Basis	0	0
Capital Gain	$1,000,000	$1,000,000
Tax (20%)	200,000	0
Net Proceeds	$ 800,000	$1,000,000
Invest at 7%		
Annual Income	$ 56,000	$ 70,000

A wealth replacement life insurance policy coupled, where appropriate, with an irrevocable life insurance trust will even more significantly increase the ultimate benefit to their heirs.

C. Often, a gift followed by a redemption by the corporation will achieve the same results. And, in corporations that have concern regarding the accumulated earnings tax, a charitable gift of stock in that corporation followed by a redemption can result in the corporation having less undistributed cash; therefore, it is less likely subject to the accumulated earnings tax and, of course, there are the other tax benefits already discussed.

D. Be careful in arranging the corporate redemption.

(1) Avoid imposition of the self-dealing rules; generally, it would appear that the corporation is itself a disqualified person that would not be able to

purchase the stock from the trust. However, Code Section 4941(d)(2)(f) provides an exception to the self-dealing rules where the corporation makes an offer on the same terms to all shareholders of the same class and the terms of the offer provide for receipt of no less than fair market value. Must be all cash deal.

E. Beware of the pre-arranged sale.

(1) The threshold case: <u>Palmer v. Commissioner</u>, 62 T.C.684(1974), Aff'd on another issue, 523 F.2d 1308(8 Cir. 1975).

(a) Donor had voting control of both a closely held corporation and a tax-exempt private foundation. Pursuant to what appeared to be a single plan, donor contributed shares of corporation's stock to foundation and then caused the corporation to redeem the stock from the foundation.

(b) IRS wanted to impute gain to Palmer.

(c) Tax Court, affirmed by the Appeals Court, held that transfer of stock to foundation was valid gift and gain not taxed to Palmer on the following grounds:

(i) Foundation was not bound to go through with redemption at the time it received title to the shares, and

(ii) Corporation's right to redeem is based upon a purchase at fair market value.

(d) IRS has acquiesced in <u>Palmer</u>. Rev. Rul., 78-197, 1978-1 CB 83. Redemption proceeds of stock under facts similar to those of Palmer will impute gain to the donor only if the donee is legally bound or can be compelled by the corporation to surrender the shares for redemption.

(2) However, see <u>Blake v. Commissioner</u>, 697, F2d. 473 (2d Cir. 1982). A "chutzpah" case.

II. <u>S Corporation Stock</u>

1. <u>Background</u>: Generally, S corporation does not pay income tax. It is a pass through entity (like a partnership) and corporation's income is taxed directly to shareholders. This avoids double taxation of income that often occurs with C corporations.

2. Charity can now be eligible S corporation shareholder. Code Section 1361(c)(6), effective January 1, 1998.

A. Charitable deduction is often less than full fair market value of stock because of reduction rule of Code Section 170(e), which requires that the income tax deduction for a gift of appreciated long-term capital gain property is generally reduced by the amount of "ordinary income" that the donor would have realized had he sold the property. With an S corporation, often Code Section 751 rules regarding certain assets such as (1) "unrealized receivables," (2) "inventory," (3) "depreciation recapture," may have impact on deductible amount.

B. Watch out for phantom income.

C. Charity will be subject to unrelated business income tax (UBIT) on its portion of S corporation's accounting income. Also, unlike almost every other capital gain asset, the gain from the sale of S corporation stock by the charity will also be subject to UBIT. Code Section 512(e)(1)(B)(ii).

3. But, the above rule does not apply to a transfer that is not an outright transfer to charity, such as a transfer to a charitable remainder trust. Such a transfer will still automatically terminate the S corporation election. Often, that can have adverse tax implications to the donor who contributes such stock.

4. A way out: S corporation creates the charitable remainder trust.

   A. S corporation transfers appreciated assets to the CRT; corporation gets the income tax charitable deduction; passes deduction through to its shareholders; problem - - deduction that can be claimed by the shareholder is limited to his or her basis in the S corporation stock which is generally minimal.

   B. But the charitable remainder trust can sell and invest the appreciated assets without capital gains tax and reinvest the full sales proceeds to generate the income stream.

   C. Trust term can only be for term of years - - not to exceed 20.

   D. Potential problems where there are multiple shareholders of the S corporation with different agendas.

III. <u>Family Limited Partnerships - - The Charitable FLP</u>

1. <u>Background</u>: Family limited partnership generally used in estate planning to manage the family wealth and create discounts for marketable securities and other assets where discounts are not generally allowable.

   A. Husband and wife, for example, create limited partnership; retain general partnership interests so that they maintain control, as well as limited partnership interests.

B. Make gifts to, say, children of limited partnership interest; take deep discounts for lack of marketability and minority interest.

C. Internal Revenue Service getting more aggressive in fighting deep discounts of, say, 50%; but the planning still works if taxpayer is not too greedy.

D. Discounts can also apply for estate tax purposes reducing the value of the estate. But, be aware, IRS using Code Section 2036 to keep value of stock in estate.

2. Charitable FLP: too good to be true? IRS has taken hard look. See Wall Street Journal article of July 13, 1999; Chronicle of Philanthropy article of July 15, 1999.

A. The mechanics.

(1) John Donor creates family limited partnership comprised of general partnership interest and one or more levels of limited partnership interests.

(2) He puts business and other appreciated assets and cash into FLP.

(3) As general partner, donor retains a management fee for operating the partnership. The fee generally ranges from 3% to 10% of partnership income. This enables donor to keep all or almost all of the firm's cash flow or, perhaps, trickle out token amount to limited partners at discretion of donor as general partner. General partner also retains the right to borrow partnership assets for personal needs at competitive interest rates.

(4) Donor makes gift of, say, 97% of limited partnership interest to charity. This generates large income tax charitable deduction.

(a) Even when majority of all the limited partnership interests are conveyed to charity, those interests carry limited, if any, control and, often, no marketability, and must, therefore, be discounted considerably for valuation of the charitable deduction.

(b) Charitable gift is made, but subject to a "put" enabling the charity to force a buyback of the limited partnership interests - - typically, at significant discount from their value when received by charity.

(5) Donor makes a simultaneous gift of remaining 3% of limited partnership units to children and/or grandchildren. Gift tax valuation of those interests also takes into account lack of control and marketability and so a relatively large valuation discount for gift tax purposes is also taken.

(6) As part of transaction, partnership purchases life insurance on donor's life to fund the later buyout. The partnership itself splits the premium dollars with an irrevocable trust representing the interests of its beneficiaries, the limited partners of the 3% interest. Therefore, indirectly, since charity holds 97% of the limited partnership interests, charity is paying most of the insurance premiums. In one variation on this theme, charity, through its "put," can sell its interest to the irrevocable life insurance trust. Thus, charity's dollars have been helping to fund life insurance that will be used to buyout its interest - - at a substantial discount - - and the trust then receives the partnership interests with a stepped up basis benefiting the family members.

Further, if there is sale of partnership assets during donor's life and before charity exercises its right to demand a purchase of its interest, approximately 97% of the gain on sale is attributable to the charitable partner. Thus, donor's family pays tax on only the 3% balance, a small fraction of the gain.

(7) At the specified "put" date, charity exercises its option to force the purchase - - at pennies on the dollar - - of the limited partnership interest charity holds. It receives cash in return for the interest, which has been sold back, either to the partnership itself or to the 3% owners or to the irrevocable life insurance trust. Thus, the family business and other holdings of the limited partnership (together with any appreciation on the relatively untaxed capital gains sheltered by the charity's exempt status) comes back into the family's control.

B. So, where's the gift? Donor and his advisors try to convince charity that it will make some money on the transaction in return for allowing the donor and his family to receive tremendous benefits from the transaction. They receive a disproportionate benefit and facilitate their personal estate planning objectives. Remember Blake? This may be another classic example of using charity to serve a private rather than public purpose.

C. The IRS' likely position.

(1) The agreement of the parties from the beginning was based on an unwritten - - but very real - - understanding between the donor and charity that, after a relatively short period of time, charity will sell its interest back to the partnership or the other partners and receive only a small portion of what the underlying assets and, therefore, the charity's limited partnership interest, is worth.

(a) IRS could argue that what charity received at the time of contribution was only the sum of the future right to receive the "put" price and the present value of minimal income distributions for, say, five years.

(b) More likely, IRS will argue that there is no allowable income or gift tax deduction because the reality is that what the donor gave was a possible but uncertain stream of dollars over a period of years.

(2) The donor and his advisors would likely argue that the "put" is merely an option and that there was never a legal obligation on the charity to sell. Therefore, the contribution of the 97% interest in the limited partnership must be respected. However, in the more egregious and aggressive cases, would the transaction ever have been entered into had the parties not "known" from the beginning that the charity would have no practical choice but to exercise its "put."

D. Does it ever work? Yes, if there is donative intent, the family limited partnership is entered into to achieve other family planning objectives and there is not the overreaching present in the type of "charitable" family partnership described above.

IV. Stock Options; Restricted Stock

1. Stock Options - - Definition: A contractual right given by a corporation to an employee (and sometimes, to an independent contractor) to purchase stock in the corporation at a stated price per share for a stated period of time. There are two basic types of options.

A. Nonstatutory ("Nonqualified") Options (IRC §83).

(1) Generally, this type of option is not taxable to an employee when granted, unless the option has a readily ascertainable value (i.e., it is actually traded on an established securities market), at the time of grant.

(2) Compensation is realized when the option is exercised or "otherwise disposed of." Compensation is equal to the difference between the fair market value of the stock at the time of exercise and the exercise price.

(3) An employee may choose to recognize compensation income on grant by making an IRC э83(b) election. Seldom done because of difficulty in ascertaining value of options. No income will then be realized on subsequent exercise.

B. Statutory Options

(1) Includes incentive stock options ("ISOs"), employee stock purchase plans, qualified stock options and restricted stock options.

(2) General Tax Treatment:

(a) The employee does not recognize taxable compensation income at the time the option is granted or at the time the option is e for

AMT purposes, the difference between the fair market value and the exercise price will be considered part of AMT income. exercised (unless exercised more than three months after leaving employment). The price for such avoidance is that the employee must not dispose of the stock until two years from the date the option was granted and one year from the date the employee received the shares upon exercise. Code Section 422(a)(1). A disposition includes a sale, exchange or gift.

(b) If the employee disposes of the stock before the holding period is up, he must recognize as compensation income the difference between the option exercise price and the fair market value of the stock at the time of the option exercise. In addition, he will recognize income equal to the difference between his basis in the stock (the exercise price increased by the amount included in gross income as compensation) and the amount he receives in the disposition.

(c) If the employee waits to dispose of the stock until after the holding period, there will be no compensation income, but there will be capital gain, if any (short or long-term, depending on how long the stock is held). The capital gain would be the difference between the amount received in the disposition over the basis in the stock (i.e., the amount the employee paid when exercising the option).

(3) Alternative Minimum Tax ("AMT") for ISOs: While the exercise of an ISO does not result in current taxable income, there are implications with regard to the AMT. When calculating income for AMT purposes, the difference between the fair market value and the exercise price will be considered part of AMT income.

(4) Where does cash for exercise come from?

(a) Other assets;

(b) Brokerage loan and sale;

(c) Sale in same year.

C. Disposition of Option Stock

(1) Definition: Generally, a disposition is any sale, exchange, gift or transfer of legal title of the stock. IRC §424(c) provides certain exceptions.

(a) Transfer from a decedent who held ISO stock to an estate, or a transfer by bequest or inheritance.

(b) Exchange of ISO stock in certain nonrecognition transactions (e.g., reorganization).

(c) Pledge or hypothecation is not a disposition, but transfer pursuant to pledge or hypothecation is a disposition.

(d) Between spouses incident to a divorce.

(e) Acquisition in joint ownership with right of survivorship. Change in joint ownership is disposition.

(f) Taxpayer in bankruptcy.

(2) IRS rulings:

(a) Purchase of a put on option stock is not a disposition (Rev. Rul. 59-242, 1959-2 C. B. 125).

(b) Short sale on option stock is a disposition (Rev. Rul. 73-92, 1973-1 C.B. 208).

D. Charitable Alternatives

(1) Outright Gift of Stock to Charity

(2) Charitable Remainder Trust

(3) Charitable Lead Trust: Employee establishes charitable lead trust with cash proceeds of sale or with other assets to offset gain in connection with exercise of option.

(4) Charitable Gift Annuity: Employee "sells" stock to charity in exchange for an annuity.

2. Rule 144 Stock

A. Regardless of whether they are publicly traded or not, securities are subject to certain Securities and Exchange Commission rules regarding their sale if they are acquired, directly or indirectly, in a transaction or chain of transactions not involving a public offering (in which case they are "restricted securities") from (1) the company issuing them or (2) an individual or company affiliated with the issuing company (generally including officers and directors of the company, in which case they are "control securities"). SEC Rule 144 provides a safe harbor for the sale of these securities if all the conditions of the rule are met.

B. Generally, Rule 144 requires that a charity and its donor together must hold restricted securities for a minimum of one year before their sale in accordance with the rule. It also imposes a value limitation on the amount of securities that can be sold by affiliates of the company during any three-month period and may require aggregation of the charity's sales with the donor's. Adequate current information on the issuing corporation must be on file with the SEC. The SEC, as well as the principal national exchange on which the securities are listed, must be notified of the sale.

C. Securities laws do not generally prohibit gift, but donor's restrictions on sale apply to donee (including charity).

D. Rule 144 stock not considered "qualified appreciated stock."

3. <u>ESOPS and CHESOPS</u>

A. ESOP is tax qualified, defined contribution employee benefit plan whereby, in return for meeting certain rules which protect the interests of plan participants, the ESOP sponsors receive various tax benefits.

B. Ordinarily, to set up an ESOP, the company creates a trust fund for employees and funds it by one, or a combination of, the following tax deductible methods:

(1) Contributing shares of the company.

(2) Contributing cash to buy company shares; or

(3) Having the plan borrow money to buy shares with the company then making payments to an ESOP trust to repay the loan.

C. Tax Advantages:

(1) Employer can deduct (within limits) contributions to an ESOP, including both principal and interest on loan proceeds the ESOP uses to buy company stock.

(2) Employer can generally deduct reasonable cash dividends, if paid to an ESOP and used to repay the ESOP loan or passed through to participants on ESOP held stock.

(3) The shareholders of a close corporation can defer taxation on the gain resulting from their sale of company stock to an ESOP, provided the ESOP owns 30% or more of a company's shares after the sale, by reinvesting sale proceeds in qualified replacement property ("QRP") consisting of stock or bonds in operating companies in the United States.

D. A CHESOP is a combination of an ESOP with a gift to charity.

(1) The simplest way is to have the shareholder donate his privately-held stock to a nonprofit institution, which then sells the stock back to an ESOP established by the company. Donor gets charitable deduction for full fair market value and avoids capital gain on the appreciation; or

(2) The owner of the shares can use the proceeds of the sale to an ESOP to purchase QRP and then gift the QRP to a qualified charity. Individual owns QRP with same holding period and basis as the stock sold to the ESOP, but avoids capital gain and gets full fair market value deduction by giving QRP to charity or, perhaps, to a qualified charitable remainder trust retaining an income stream.

V. Gifts of Real Estate

1. Real estate represents approximately 50% of total individual wealth; important that charities tap potential of real estate gifts.

2. Many kinds of real estate interests; know the names and rules, for example: whole fee interests; partial interests (undivided interests, life estate and remainder; joint tenancy; tenancy in common).

3. Income tax charitable contribution deduction.

A. Limit on charitable deduction for appreciated real estate gifts is 30% of adjusted gross income with five year carryover for any "excess" contribution - - up to 30% of adjusted gross income in each carryover year until exhausted.

B. If you can't use entire gift, consider contributing partial or undivided interest over a period of years or making the election to reduce the amount of the gift by the appreciation so that the ceiling increases to 50% of adjusted gross income.

4. Transfer of Encumbered Property to Remainder Trusts and as Outright Gift.

A. Mere transfer of mortgaged property is deemed bargain sale. Reg. Section 1.1011-2(a)(3).

(1) IRS has said Reg. Section 1.1011-2(a)(3) applies to CRT. Rev. Rul. 81-163, 1981-1 C.B. 433.

(2) Gain is for difference between amount of debt and allocated adjusted basis; not limited by property's fair market value.

B. LTR 9015049. CRT disqualified if funded with mortgaged property.

(1) Facts. D planned to fund charitable remainder unitrust with income-producing real estate. Trustee would make regularly scheduled payments on mortgage, but D would remain personally liable for the debt.

(2) IRS rules. Trust won't qualify. Charitable remainder trust must function exclusively as one from its creation. It isn't charitable remainder trust - indeed, it isn't even deemed "created" - as long as donor treated as owner of entire trust under the grantor-trust rules. Reg. Section 1.677(a)-1(d) provides that donor is treated as owner of trust whose income is or may be applied in discharge of donor's legal obligation. Because D would be treated as owner of entire trust, it wouldn't be deemed "created," and thus wouldn't qualify as charitable remainder unitrust.

(3) Earlier rulings (i.e. LTR 8931023).

C. Possible ways to avoid issue:

(1) If outstanding mortgage is small, donor may be willing to satisfy it before transferring property to trust.

(2) Sometimes lender may be willing to release mortgage if donor can substitute other security for indebtedness.

(3) Donor could sell undivided interest in property to charity (reporting capital gain on any appreciation attributable to that interest). Then donor could use sale proceeds to satisfy mortgage, and transfer unencumbered property to charitable remainder trust. Charity would have to take care not to pay more than fair market value for undivided interest - and fractional interests in property may have to be discounted to reflect the unwieldiness of a co-tenancy arrangement. Naturally, charity would first have to be sure charitable remainder is large enough to make it all worthwhile.

5. Gifts of personal residence with retained life estate.

A. Charitable deduction (for income, gift and estate tax purposes) allowed for gift of remainder interest in real property (not made by transfer to charitable remainder unitrust, annuity trust or pooled income fund trust) only if remainder interest is in personal residence or farm.

B. Life tenant (often donor) must maintain property --- pay real estate taxes, insurance premiums and for ordinary repairs.

6. Bargain Sale.

A. Real estate is sold to charity for below fair market value; difference between fair market value and sales price is charitable contribution deduction.

B. Donor's cost basis is allocated on a pro rata basis between sale and gift portion. The gain attributable to the sale portion is realized by the donor; the appreciation attributable to the gift portion is not taxed.

C. Intention to make a gift should be well documented.

7. Gift of Land for Conservation Use.

A. Gift of lease, option to purchase or easement as to real estate that is granted in perpetuity qualifies for the charitable deduction as long as the gift is made exclusively for conservation purposes. See Code Section 170(f)(3)(B)(ii).

B. Value of easement is its fair market value on date of gift. If there is no meaningful record of market place sales, then the value of the easement and, thus, the deduction equals the difference between the pregift fair market value and the post gift fair market value of the entire property.

C. No deduction allowed if the grant of the easement may have no material effect on property's value or may enhance, rather than reduce, property's value. Regulation Section 1.170A-14(h)(3)(ii).

D. The amount of basis that is allocable to the qualified conservation interest is in the same ratio to total basis as to the fair market value of the contributed interest bears to the fair market value of the property before the gift.

VI. Gifts of Tangible Personal Property

1. Deductibility of gift of tangible personal property (for example, art or other collectibles) deductible at fair market value only if gift is deemed as being made for a related use. If gift is being deemed for an unrelated use, gift is limited to cost basis.

2. See special rule of Code Section 170(a)(3) below.

3. Transfer of Tangible Personal Property to Remainder Trusts. Is A Puzzlement!

A. Code Section 170 (a) (3):

Future Interests in Tangible Personal Property -- For purposes of this section, payment of a charitable contribution which consists of a future interest in tangible personal property shall be treated as made only when all intervening interests in, and rights to the actual possession of enjoyment of, the property have expired or are held by persons other than the taxpayer or those standing in a relationship to the taxpayer described in section 267(b) or 707(b). For purposes of the preceding sentence, a fixture which is intended to be severed from the real property shall be treated as tangible personal property."

B. The Krugerrand Rulings:

(1) LTR 9225036 held that appreciated in value Krugerrands are more like money than collector's coins (tangible personal property), thus the deduction for a transfer to a CRT would be based on full fair market value -- not cost. The Service also said that funding an otherwise qualified CRT with Krugerrands would not disqualify the trust. And, since the coins were not tangible personal property, the rules of IRC Section 170 (a)(3) won't apply.

(2) A second Kruggerand ruling submitted some nine months later, which was withdrawn because of the tax payer's death, appeared to indicate that IRS had changed its mind.

C. LTR 9452026 held that funding a CRT with an appreciated musical instrument is OK.

(1) IRS did not rule on the qualification of the trust referring to its Revenue Procedures containing specimen CRT documents.

(2) Since the instrument is tangible personal property, no income tax deduction is allowed under IRC Section 170 (a) (3). A deduction is allowed only when it is sold.

(3) It's an unrelated use gift and, therefore, the income tax contribution deduction is based on cost, not fair market value.

D. A dilemma, what to do?

VII Valuation and Substantiation Rules

1. Valuation -- General Rules.

A. Basics. If a charitable contribution is made in property other than money, the amount of the contribution is the fair market value of the property at the time of the contribution... fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.

B. Comparable sales.

(1) Comparable sales technique (also known as "market data method") most useful when donated property similar to other property available on open market.

(2) Appraiser locates several similar items -- called "comparables" -- that were sold or available for purchase near time of donation.

(3) That gives ballpark figure. Then value increased or decreased, depending on how donated property stacks up against comparables.

C. Capitalization of income.

(1) If asset generates income, value can sometimes be appraised by estimating how much income it can be anticipated to earn.

(2) Then match to market rates.

D. Replacement cost.

(1) This method most often used when property to be valued is unique and isn't expected to generate income.

(2) Because replacement cost represents value of brand-new asset, adjustments may be made to reflect depreciation on property before its donation.

E. Subsequent sales.

(1) Often, charities that have no immediate use for donated property sell property and use sales proceeds for charitable endeavors. Although sale price of donated asset is not conclusive evidence of fair market value, IRS and the courts generally find it very persuasive.

(2) Indeed, new reporting requirements for certain contributed property sold within two years of gift show how probative Congress finds that information.

2. Form 8283: Appraisal summary.

3. Form 8282: The "tattle tale" form.

4. Appraisals.

A. What must be appraised?

(1) Property gifts (other than money and publicly traded securities) if claimed or reported value of property exceeds $5,000. To determine whether $5,000 threshold crossed, only part of gift claimed as charitable deduction counts. Thus, if land worth $25,000 is placed in charitable

remainder unitrust, appraisal requirements apply only if charity's remainder interest more than $5,000 and donor claims income tax charitable deduction.

(2) What is "qualified appraisal"?

(a) Qualified appraisal can be done any time from 60 days before donation up until due date (including extensions) for return on which donor reports or claims gift; post-donation appraisals are okay.

(b) Regulations require qualified appraisal to give following information:

(i) Description of property in sufficient detail for person who is not generally familiar with type of property to ascertain that appraised item is property contributed.

(ii) In case of tangible property, its physical condition.

(iii) Date (or expected date) of contribution to donee-charity.

(iv) Terms of any agreement or understanding entered into (or expected to be entered into) by or on behalf of donor (or donee) that relates to use, sale or other disposition of contributed property; includes, for example, terms of any agreement or understanding that –

(A) Restricts (temporarily or permanently) donee-charity's right to use or dispose of donated property;

(B) Reserves to, or confers upon, anyone (other than charity or organization participating with charity in cooperative fund-raising) any right to income from donated property or possession of property - including right to vote donated securities, to acquire property by purchase or otherwise, or to designate person having income, possession, or right to acquire; or

(C) Earmarks donated property for particular use.

(v) Name, address and TIN of qualified appraiser (or appraisers) and - if qualified appraiser is a partner in partnership, employee of any person (whether individual, corporation, or partnership or independent contractor engaged by person other than donor - name, address and TIN of partnership or person who employs or engages qualified appraiser.

(vi) Qualifications of appraiser who signs appraisal, including appraiser's background, experience, education, and membership, if any, in professional appraisal associations.

(vii) Statement that appraisal was prepared for income tax purposes.

(3) Provisions of Pension Reform Act of 2006 tighten rules.