THE SALVATION ARMY

# Charitable Intent

DOING THE MOST GOOD

PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

## BENEFICIARY REQUIRED TO WAIT FOR UNITRUST

Cyndi Neal-Lunsford was named the income beneficiary of a $2.4 million charitable remainder unitrust established by Burnham Neal. Neal's will provided that, until full funding of the trust, assets awaiting distribution were not to be taken into account in determining the unitrust amount.

On December 2, 2013, the trustee received a single payment of $2.4 million from Neal's estate. The following month, Lunsford filed a petition to construe the trust, asserting that, under the Illinois Principal and Income Act, she was entitled to income beginning at Neal's death. She estimated that she was entitled to nearly $140,000 for the period between his death on April 12, 2012, and the full funding of the trust.

The trial court ruled that where the trust instrument provides a date upon which the obligation to pay is to begin, the trust language supersedes the Principal and Income Act. The court found that the "plain language" of Neal's will directed that the unitrust obligation was dependent on the full funding of the trust.

The Appellate Court of Illinois affirmed, noting that because the trust instrument "sufficiently identified funding of the unitrust" as the event for the beginning of the obligation to pay, Lunsford was not entitled to income from the period between Neal's death and the trust's funding. ***In re Estate of Neal*, 2015 IL App (4th) 140293-U**

**▲ Tax Planning Pointer**

Neal's estate would not be entitled to a charitable deduction for the value of charity's remainder interest because, under Rev. Rul. 72-395 and Reg. §1.664-1(a)(5)(i), an estate tax deduction is allowable for a testamentary transfer to a charitable remainder trust only if the obligation to pay the annuity or unitrust amount with respect to the property transferred begins as of the date of the decedent's death.

## ESTATE SHOULD HAVE KNOWN MONEY WOULD BE SPENT

The estate of Eileen Belmont claimed a $219,580 charitable deduction on its 2008 income tax return for funds permanently set aside during the taxable year for charitable purposes [Code §642(c)(2)]. Under the terms of Belmont's will, her brother was to receive $50,000 from the residue, with the balance passing to a charity.

One of the assets owned by Belmont was a condominium in California. Her brother, David, had moved into the unit about nine months prior to Belmont's death. David filed suit in the probate court asserting that he had a life tenancy on the basis of a "resulting trust" theory. The estate argued that David had no ownership interest in the condo. The probate court judgment in favor of David was upheld by the appellate court.

The estate incurred expenses related to the probate litigation and appeal and had to invade some of the $219,580 that had been set aside for charity. The IRS disallowed the estate's income tax deduction, saying that the funds were not "permanently set aside for charitable purposes." Under Reg. §1.642(c)-2(d), an amount is not considered permanently set aside unless the possibility that the funds will not be devoted to a charitable purpose is "so remote as to be negligible." The estate argued that there was no "reasonably foreseeable possibility" that it would incur the costs due to the litigation.

The Tax Court noted that David's legal claims were initiated prior to the estate filing the income tax return. Therefore, the estate was on notice that "an extended and expensive legal fight" might ensue, leading to an invasion of the funds set aside for charity. That possibility was not so remote as to be negligible, said the court, which denied the estate's deduction. ***Estate of Belmont v. Commissioner*, 144 T.C. No. 6**

## EASEMENT MUST STAY IN PLACE

Balsam Mountain Investments conveyed a conservation easement over a specific 22-acre parcel of land in North Carolina to the North American Land Trust. The boundaries of the easement were set forth in a plat attached to the easement agreement. The stated goal of the easement

was the preservation of the area as a natural habitat and open space.

Balsam reserved the right to make "minor alterations" to the exact boundary, providing several requirements were met. Among these: the total land area would not be reduced, land added to the easement would be contiguous to land in the original easement, the Land Trust would have to find the alteration to be of equal or greater value than any land removed, the total land subject to the alteration would not exceed 5% of the original area and no changes could be made after five years.

The IRS disallowed the charitable deduction on the grounds that the easement was not a "qualified real property interest," as required under Code §170(h)(2)(C), and therefore not a qualified conservation contribution. The Tax Court agreed with the IRS, noting that an interest in real property is a qualified real property interest only if it is an interest in an "identifiable, specific piece of real property." ***Balsam Mountain Investments, LLC v. Commissioner***, **T.C. Memo. 2015-43**

## CHARITABLE DEDUCTION CARRYOVER TRIGGERS PENALTY

In 2004, Edward Reisner and Manda Weintraub granted a facade easement to the National Architectural Trust on their Brooklyn townhouse. The couple claimed a charitable deduction of $190,000, a portion of which was carried forward to their 2005 and 2006 tax returns.

The IRS challenged the valuation, and the taxpayers eventually stipulated that the 2004 easement had zero value. The IRS said the donors were not subject to a penalty under Code §6662(h)(2)(A) for a gross valuation misstatement for 2004 or 2005, because they satisfied the reasonable cause exception. Code §6664(c)(1) provides that no penalty is imposed if the taxpayers acted in good faith. However, the IRS said they were subject to the penalty for the carryover to 2006. The Pension Protection Act of 2006 eliminated the reasonable cause exception entirely for underpayments attributable to gross valuation overstatements of charitable deduction property on returns filed after July 25, 2006.

The donors argued that Congress provided that amendments to the conservation easement rules were to apply to "contributions made" after July 25, 2006. The timing of the contribution, rather than the filing of a return claiming the deduction, was the intent, they argued. The Tax Court acknowledged that amendments to Code §170(h)(4) were effective for gifts made after July 25, 2006, but the provision eliminating the reasonable cause exception for underpayments was made effective for "returns" filed after July 25, 2006. Congress "clearly intended a distinction," said the court. ***Reisner and Weintraub v. Commissioner***, **T.C. Memo. 2014-230**

## USING IRA TO SATISFY BEQUEST AVOIDS TAX ON IRD

A decedent's will provided that the residue of the estate was to be paid to a trust. The trust included two pecuniary bequests, with the remaining trust property to be immediately distributed to charity. The trust was also the primary beneficiary of the decedent's IRA. The estate and trust plan to assign and transfer the IRA directly to charity and asked the IRS to rule on whether it would be a transfer within the meaning of Code §691(a)(2).

The term "transfer" includes a sale, exchange or other disposition, but does not include transmission at death to the decedent's estate or a person receiving a bequest, devise or inheritance from the decedent.

The IRS ruled that if the trust retitled the name of the IRA, it would not constitute a payment or distribution out of the IRA to the estate, trust or charity and will be a nontaxable transfer. The retitling will not be a transfer under Code §691(a)(2). The charity will include the amount of income in respect of a decedent when distributions from the IRA are received, although the charity will pay no tax, thanks to its tax-exempt status. ***Letter Ruling 201444024***

**KEEP THE SALVATION ARMY IN MIND**

It's understandable that family members come first when clients consider how to distribute their estates, even those who contributed generously to charity during their lifetimes. But there are ways to provide for charitable organizations while giving consideration to family members. Every will can, and probably should, include language allowing named beneficiaries to disclaim in favor of selected charities. This gives named beneficiaries the opportunity to direct part or all of a bequest as a memorial for the deceased, while qualifying for an estate tax charitable deduction. Another option is to name charity as a contingent beneficiary, in the event a named beneficiary has predeceased the decedent. This, too, qualifies for a charitable deduction and avoids having estate assets pass to distant relatives – or the state. For more information about these and other bequest options, or for our correct legal name, please feel free to call The Salvation Army.