THE SALVATION ARMY

Charitable Intent

Doing the Most Good

PLANNING NEWS AND IDEAS FOR THE PROFESSIONAL ADVISER

SELF-DEALING RULES AVOIDED BY FORGOING DEDUCTION

A grantor funded a charitable remainder unitrust that is to last for his lifetime and then continue for the longer of 20 years or the lifetime of a successor beneficiary. No charitable deduction was claimed for the value of the remainder interest of the unitrust.

The IRS ruled that, because no deduction has ever been taken, the trust is not subject to the private foundation rules of Code §4947(a)(2), even though a deduction was allowable. The purpose of Code §4947 is to prevent the use of nonexempt charitable trusts to avoid the restrictions, such as self-dealing, imposed on private foundations. The IRS said the grantor will have to keep records showing that no deduction was taken during the life of the trust. **Letter Rulings 201713002, 201713003**

FOREIGN CHARITY MEETS CHARITABLE REQUIREMENTS

An American citizen included a bequest in her will leaving property located in a foreign country to a charity in that country. The bequest was contingent on the organization, which works to improve the quality of life of the handicapped and elderly, satisfying the requirements of Code §2055(a).

Reg. §20.2055-1(a)(4) provides that the estate tax charitable deduction is not limited to transfers for use within the U.S. The charity must be organized and operated exclusively for religious, charitable, scientific, literary or educational purposes, and no part of the net earnings may inure to the benefit of a private individual.

The IRS noted that the charity is operated by a board of directors who are subject to the organization's code of ethics and good governance. The earnings may not benefit any individual, and the organization's assets cannot be used for lobbying. The charity does not engage in any prohibited transactions within the meaning of Code §4948(c). Therefore, the IRS ruled, the bequest was made to an organization described in Code §2055(a)(2) and the estate is entitled to a charitable deduction. **Letter Ruling 201702004**

▲ Tax Planning Pointer

For *income tax* purposes, only organizations "created or organized in the U.S." qualify for a deduction, although gifts to domestic charities that have foreign operations may be allowed if the charity maintains control over the use of the funds [Rev. Ruls. 63-252, 66-79].

GOOD NEWS: NO GIFT TAX. BAD NEWS: INCLUDED IN ESTATE

Two days after establishing NHP, a limited partnership, assets worth more than $10 million were transferred in exchange for a 99% limited partnership interest for Nancy Powell. The same day, Powell's son, acting under a power of attorney, transferred her interest to a charitable lead trust that was to pay a fixed amount to a private foundation for Powell's life. At her death, assets from the lead trust were to be divided equally into trusts for Powell's two sons. Powell died one week later.

The gift tax return valued the remainder interest to the sons at $1,661,422. The IRS said that because Powell was terminally ill when the transfer to the lead trust was made, the value of the remainder was $8,363,095. The IRS also said that the value of the trust was included in her gross estate, either because she retained the enjoyment or right to the income from the property she transferred [Code §2036(a)] or she retained at her death a power to change the enjoyment of the transferred property [Code §§2038(a), 2703(a)].

The Tax Court found that under state (California) law, the gift was either void or revocable because Powell's son did not have the authority under the power of attorney to make gifts in excess of the annual exclusion amount. In addition, even if the transfer was valid under state law, because it was made within three years of Powell's death, the value would be included in her estate under Code §2035(a). The court granted the IRS's motion for summary judgment that the transfer to NHP was subject to a retained right to designate the persons who shall possess or enjoy the assets or the income [Code §2036(a)(2)]. Because the value of Powell's interest in NHP was included in her gross estate, the gift to the lead trust was either void or revocable. Therefore, said the court, the estate is not liable for the gift tax deficiency. ***Estate of Powell v. Commissioner*, 148 T.C. No. 18**

VOLUNTEER NOT ALLOWED TO HAVE "FUN"

Edgar Brown traveled to North Carolina to participate in a soccer tournament staged annually by the Julian Brown Memorial Fund, which he established in 2005. He stayed in a house that he owned near the tournament. Brown initially claimed a charitable deduction of $9,200 – later reduced to $901 – for expenses related to his volunteer work for the fund.

Unreimbursed expenditures incident to volunteer services may be deductible [Reg. §1.170A-1(g)], provided they are directly connected with and solely attributable to the rendering of services to charity. Code §170(j) provides that no deduction is allowed for travel expenses – including meals and lodging – while away from home unless there is no significant element of "personal pleasure, recreation or vacation."

The Tax Court disallowed the deduction for Brown's travel expenses, saying he failed to explain what he did for the soccer tournament or how much time he devoted to it. The court did, however, allow Brown to deduct $490 for expenses incurred in maintaining the fund's website. All of the expenditures were less than $250 and could therefore be substantiated with a reliable written record. Brown's written summary of expenses showed the date and amount, along with the name of the payee, noted the court. ***Brown v. Commissioner*, T.C. Summ. Op. 2017-29**

COURT: WE KNOW WHAT SHE MEANT

Ellen Bruce gave her daughter, Louise, the testamentary power to appoint the balance in two trusts to any person other than her "creditors, her estate or the creditors of her estate." If Louise failed to exercise the power, the remainders would pass to other relatives.

Louise's will exercised the power of appointment by having the property added to her residuary estate. The will then directed the executor to create a foundation in her name, to be funded with the residue of the estate. Ellen's relatives argued that by appointing the property to her estate, Louise exceeded her authority.

The Surrogate's Court of New York County read Louise's will to direct the trustees to distribute the remainders to the executor of her estate, not as an agent of Louise's estate, but as the agent of the foundation that her will directed him to establish. The court called the wording "inartfully expressed," but concluded that it was a valid exercise of Louise's power of appointment. ***In re Will of Bruce*, 2017 NY Slip Op 30967(U)**

NOT REIMBURSED OR DEDUCTIBLE

No charitable deduction is allowed for volunteer services, but unreimbursed expenses can be claimed [Reg. §1.170A-1(g)]. They must be substantiated in generally the same manner as cash gifts. For expenses of less than $250, a canceled check, receipt or other reliable written record, showing the name of the payee, date and amount of the payment, is sufficient. A contemporaneous written acknowledgment from the donee organization is required for expenses of $250 or more.

Adolph Martinez claimed unreimbursed volunteer expenses of $7,000 and $5,825 for 2012 and 2013 respectively, some of which were in excess of $250. He produced a letter from the charity, dated June 1, 2015, indicating he was a volunteer and was not reimbursed for expenses. The Tax Court denied the deduction, saying the letter was not contemporaneous. ***Martinez v. Commissioner*, T.C. Summ. Op. 2017-42**

THE BOOMERS ARE GRAYING

The leading edge of the Baby Boomer generation – those born from 1946 to 1964 – started turning age 70½ last year and will be coming face-to-face with required minimum distributions from IRAs and 401(k) plans. This may provide an incentive for clients to review investments and retirement planning, for those not already retired. Many may find they don't need all the funds they are required to take from retirement accounts and, in fact, resent the income tax they have to pay on the withdrawals. Those who are philanthropically inclined should be reminded – before taking the full required minimum distribution – that there are tax savings available for making qualified charitable distributions (QCDs) from IRAs. While there's no income tax charitable deduction allowed, the QCD can take the place of required distributions and avoid the tax that would otherwise be paid. Even amounts in excess of the required minimum distribution pass tax-free, up to $100,000 annually, and can reduce the size of IRAs, resulting in lower required distributions in future years. We'd be happy to answer any questions about how QCDs can benefit clients. Please feel free to call our office.