

The Advisor



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ESTATE PLANNER'S TIP

Clients who don't need required minimum distributions from IRAs to live on often wait until late in the year to make withdrawals, allowing the tax-sheltered growth to continue as long as possible. Since 2006, IRA owners ages 70½ and older could make direct transfers of up to \$100,000 from their IRAs to charity and avoid the income tax that would otherwise be owed on funds taken out each year. These qualified charitable distributions (QCDs) took the place of required minimum distributions. Although no charitable deduction was available, clients could nevertheless save taxes. QCD legislation expired at the end of 2014 and, while it might be renewed later this year, it leaves philanthropic clients in limbo. One suggestion for clients who generally itemize their deductions and who also contribute to charity is to have the custodian of their IRAs make gifts directly to charity, up to the amount of their required minimum distributions. If the law is reinstated, as it has been several times, these transfers will retroactively qualify as QCDs. If the law is not renewed, the clients will owe the tax that would normally be due on their distributions, but they will then be entitled to income tax charitable deductions. In both 2013 and 2014, the legislation was renewed late in December, after many donors had already taken their required distributions.

FINAL PORTABILITY RULES ISSUED

The IRS has issued final regulations regarding the portability of a deceased spousal unused exclusion (DSUE) amount, effective June 12, 2015. Under Code §2010(c), the estate of a decedent who is survived by a spouse can make a portability election allowing the surviving spouse to apply the DSUE amount to the surviving spouse's own transfers during life and at death.

In general, a portability election is effective only if made on an estate tax return filed by the executor of the decedent's estate within the time

prescribed for filing such returns. Temporary regulations require estates electing portability to file an estate tax return within nine months of the decedent's date of death, unless an extension of time for filing has been granted. In response to comments, the IRS said that final regulations provide that an extension of time to elect portability will not be granted under Reg. §301.9100-3 to any estate required to file an estate tax return because the gross estate equals or exceeds the threshold amount (\$5.43 million in 2015), but may be granted to estates with a value below the threshold

amount that were not otherwise required to file an estate tax return.

The IRS also said that final regulations do not provide for the filing of a protective election where the DSUE amount is uncertain, noting that the computation requirement in Code §2010(c)(5)(A) will be satisfied if the estate tax return is filed in accordance with Reg. §20.2010-2(a)(7). This applies where an estate becomes entitled to a deduction under Code §2053 for a payment made in satisfaction of a claim against the estate that reduces the estate tax and results in an unused exemption (T.D. 9725).

RULING SERVES AS REMINDER FOR OTHERS

Debra created two charitable lead annuity trusts that were to pay charity for a period of years before the trust assets passed to the named individuals. In each case, the valuation of the charitable interest was determined using the §7520 rate from the month two months prior to the month of the transfer.

Form 709, U.S. Gift (and Generation-Skipping Transfer) Tax return was filed for each of the transfers, although the statement and information required under Reg. §25.7520-2(b) for making a prior-month election in determining the value of the charitable interest was not included.

PHILANTHROPY PUZZLER

It wasn't until after he was named executor of his uncle's estate that Fred discovered that the charitable remainder trust created in the will was defective. The trust was to pay a 5% annuity income to Fred for life, with the remainder divided between charity (75%) and Fred's children (25%). Fred has asked if anything can be done to salvage the charitable deduction.

Debra, who relied on her attorney and CPA to file the returns, asked the IRS for an extension of time to file an amended Form 709 to make the prior-month election.

A taxpayer is required to make a prior-month election by attaching the information to the gift tax return or to an amended return filed within 24 months. The month that is being elected must be identified [Reg. §25.7520-2(b)(2)]. The IRS has the discretion to grant a reasonable extension of time to make an election if the taxpayer has acted reasonably and in good faith and if granting the relief will not prejudice the IRS [Reg. §301.9100-3(a)]. The IRS ruled that Debra had met these requirements and granted a 120-day extension to file an amended return making the election (Ltr. Rul. 201518007).

COURT: OKAY FOR DONOR TO TALK ABOUT BARGAIN SALE

Bob Davis learned that the Sears Methodist Retirement System (SMRS) was looking for property on which to establish a retirement community in the Waco, TX, area. Davis was a real estate investor and philanthropist in the area.

In 2005, SMRS approached Davis about donating a specific parcel for the retirement community. Davis indicated he could not contribute the entire parcel and SMRS said it could not afford to pay more than \$2 million. SMRS suggested that Davis might be entitled to a charitable deduction for a bargain sale if he sold the land for less than fair market value. The parties eventually agreed to a \$2 million purchase price, provided the land was appraised at \$4.1 million. The appraiser placed a market value of \$4.1 million, assuming the entire tract could be zoned for multifamily use.

The sales agreement provided that Davis was selling the land to SMRS's foundation in a bargain sale. SMRS provided Davis with a letter, thanking him for his gift of property valued at \$4.1 million for a sale price of only \$2 million.

Davis filed Form 8283, reporting the \$2.1 million bargain sale gift. The IRS denied the entire deduction, saying that Davis lacked charitable intent, that he failed to substantiate the gift and that the fair market value of the land at the time of the sale did not exceed \$2 million.

The Tax Court found that at the time of the sale, Davis believed he was selling the land for less than fair market value and that he intended the excess value to be a charitable gift. The mere fact that SMRS suggested the idea of a bargain sale and that Davis discussed it with his accountant does not mean that he lacked charitable intent.

The court also found that the letter from SMRS, stating the appraised fair market value and the sale price, was a contemporaneous written acknowledgment within the meaning of Code §170(f)(8)(A). The statement regarding the amount of money paid satisfied the requirement that the substantiation include a description of goods or services provided in exchange for the gift (*Davis v. Comm’r.*, T.C. Memo 2015-88).

CHARITY LACKS STANDING

During Robert David Lion Gardiner’s life, he allowed the Sagtikos Manor Historical Society to give tours of and to maintain his historic manor house. In 1985, Gardiner established a charitable foundation in his name to which he conveyed the manor. The foundation’s purpose was to educate and inform the public about the history of Islip, NY, and surrounding area, and to encourage and sponsor existing and future historical societies regarding the area’s heritage and traditions. In 2002, the foundation sold the manor to Suffolk County, which entered into a custodial agreement with the Historical Society for maintenance and preservation of the manor in 2005.

Gardiner died in 2004, directing in his will that at his wife’s death, the principal in a residuary trust was to be distributed to the foundation. At the wife’s death in 2011, the residuary trust contained about \$81 million.

The Historical Society requested an accounting from the foundation. The foundation refused, saying that the Historical Society was not a beneficiary under Gardiner’s will or trust.

The Appellate Division of the Supreme Court of the State of New York noted that the state’s attorney general represents beneficiaries of bequests for religious, charitable, educational or benevolent purposes and has the right to enforce beneficiaries’ rights. A party with a “special interest” also may have standing. This generally involves a class of intended beneficiaries that is entitled to preference and is limited in number, said the court. It is not an organization that is merely a “possible beneficiary” or member of a class of possible beneficiaries.

The court noted that neither the foundation’s certificate of incorporation nor Gardiner’s will name the Historical Society as a beneficiary, meaning that it lacks standing to enforce an action for an accounting (*Sagtikos Manor Historical Society, Inc. v. Robert David Lion Gardiner Foundation*, 2015 NY Slip Op 3342).

PUZZLER SOLUTION

The uncle’s trust would have qualified for an estate tax charitable deduction but for the requirements of Code §2055(e)(2) that it be a qualified annuity trust or unitrust. Therefore, it is reformable under Code §2055(e)(3). The interests of the parties will be identical if two trusts are created – one funded with 75% of the assets and the other with 25% and with Fred the income beneficiary of both. At his death, the remainder of the larger trust will pass to charity. The estate will be entitled to a deduction for charity’s remainder interest in that trust (Ltr. Rul. 9529042).

SUPPORT MOM, DAD AND FAVORITE CHARITIES

Many Gen Xers, just like the Baby Boomers before them, are finding themselves responsible for the care of elderly parents. For some, the obligation can be coupled with charitable giving to ease the financial burden. Grown children may be able to claim the parents on their income tax return [Code §152(a)] if they provide more than half the parent's support and the parent's annual gross income (not including tax-exempt income) is less than \$4,000 (in 2015).

If several siblings provide support for the same parent, only one child may claim the deduction. That child must pay at least 10% of the parent's total support and together the siblings must satisfy the 50% of support test. The children can sign a multiple support agreement designating which child is entitled to claim the deduction [Code §152(c)].

Often a child is not able to claim a parent, either because the parent's income is too high or because several siblings are contributing to the parent's support. It may be possible to structure a charitable gift that provides income for the parent, a deduction for the child and support for a favorite organization.

For example, Kevin helps support his 72-year-old father by contributing \$250 per month (\$3,000 annually). Assuming Kevin is in the 28% tax bracket, he has to earn almost \$350 to make the \$250 per month after-tax contribution to his dad. He could instead create a 5% charitable remainder unitrust and enjoy the following financial benefits (assuming quarterly payments and a 2% §7520 rate):

Amount Transferred	Annual Payments	Charitable Deduction	Tax Savings
\$60,000	\$3,000	\$33,239	\$9,307

Kevin could replace the payments he currently

makes to his father while saving significant taxes, both with the charitable deduction and by removing from his gross income the income earned each year on the \$60,000 that was transferred to the charitable remainder trust. The value of his father's interest – \$26,761 – would be completely sheltered from gift tax by the \$14,000 annual exclusion [Code §2503(b)] and Kevin's gift tax credit. If Kevin decided to increase the payments, he could simply make an additional contribution to the unitrust, for which he would be entitled to another charitable deduction. Not only has he shifted the obligation to pay \$250 to his father each month, Kevin is also relieved of the worry of providing funds should his own financial situation change as he gets older.

If Kevin has highly appreciated securities with which to fund the trust, he could also benefit by avoiding the capital gains tax that he might have to pay on the sale of the assets. Kevin also could name himself as the successor beneficiary of the trust, although his charitable deduction would be reduced to \$14,522, assuming he is age 50.

Another option for Kevin is to arrange a charitable gift annuity with a favorite charity. The recommended gift annuity rate for an individual his father's age is 5.4%, meaning Kevin could transfer even less – \$55,000 – to provide his father with reliable annual lifetime payments of nearly the same amount (\$2,970) that he is currently contributing. The value of his father's annuity interest would be \$32,673, still completely sheltered from gift tax. The charitable deduction of \$22,327 saves Kevin taxes of \$6,252. Most satisfying for Kevin, of course, is knowing that after his father's death, the funds will be used to benefit a worthwhile organization.

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