

The Advisor



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ESTATE PLANNER'S TIP

Appraisals may be needed for gift tax purposes, even for gifts that seemingly fall within the \$14,000 annual exclusion [Code §2503(b)], if there is a chance the gift value will be challenged by the IRS. Because no gift tax is paid and no return is filed, the three-year statute of limitation does not begin running, giving the IRS unlimited time to readjust the value of the gift. It's particularly important that clients obtain qualified appraisals where closely held stock, tangible personal property, partial interests in real estate or other hard-to-value property is involved, to bolster the client's position in the event the IRS questions the value years later. Even where the gift exceeds \$14,000 and a return is filed, the use of the gift tax credit does not constitute payment or an assessment of the gift tax that will prevent an adjustment under Code §2504(c) (Rev. Rul. 84-11). For a gift to be adequately disclosed to the IRS, the return must include a description of the property and any consideration received by the donor, the tax identification number if the gift is transferred to a trust and the disclosure of any relationship between the donor and transferee. There must also be either a detailed description of the method used to value the asset or an appraisal by a qualified appraiser.

MISSING MONEY SUBJECT TO TAX

While he and his wife were in the process of a divorce in 2011, Barry Skog withdrew \$45,000 from his wife's IRA. He claimed the funds were transferred into an irrevocable trust for the benefit of his daughter, although the Tax Court found nothing in the trust's paperwork naming her as a beneficiary. The trust's investment accounts showed no deposits during 2011.

The IRA rollover exception [Code §408(d)(3)(A)] allows a taxpayer to exclude from income any amount withdrawn from an IRA if rolled over into another qualifying retirement

account within 60 days. The rollover account must be for the benefit of the individual for whom the original account was maintained.

The court said it did not know where the money went, but it did not go into an account for his soon-to-be ex-wife, it was not transferred within 60 days of the withdrawal and the trust was not a qualifying retirement account. The court agreed with the IRS that Skog was subject to tax on the withdrawal (*Skog v. Comm'r.*, T.C. Memo. 2016-210).

NO MULLIGAN FOR DEDUCTION

PBBM-Rose Hill, Ltd. claimed a charitable deduction of \$15 million for a conservation easement over 234 acres of a golf course. Several days after the contribution, PBBM sold the course to the adjacent homeowners' association for \$2.3 million. The IRS disallowed the deduction.

PBBM told the Tax Court that the value of the easement was \$13,380,000; the IRS said it was worth \$100,000. The court found PBBM was not entitled to the deduction for two reasons, other than valuation.

Reg. §1.170A-14(g) requires that to comply with the perpetuity requirements of Code §170(h)(5)(A), the easement must provide that in the event a conservation restriction is extinguished by a judicial proceeding, a proportionate share of the proceeds must pass to the charitable holder of the easement. The agreement between PBBM and the North American Land Trust (NALT) instead set forth a formula. The court found that because NALT might not receive the amount required by the regulations, PBBM was not entitled to a charitable easement.

The court also found that a significant portion of the property subject to the easement was inaccessible to the general public. Reg. §1.170A-14(d)(4)(ii)(A) requires that the preservation must yield a "significant public benefit." The court said the owners of houses abutting the golf course were the main beneficiaries of the easement.

The court reduced the charitable deduction to \$100,000, noting that if PBBM had thought the development potential of the property was worth the \$15 million claimed as a charitable deduction, it would not have sold the golf course land to the property owners for only \$2.3 million (*PBBM-Rose Hill, Ltd. v. Comm'r.*, 2016ARD 201-1).

COURT FINDS "NO BASIS" FOR IRS'S VALUATION

Both the Tax Court and U.S. Court of Appeals (11th Cir.) agreed with the donor that the highest and best use of real property over which a conservation easement had been created was residential. That determination was necessary to apply the before-and-after method for valuing the charitable deduction. Palmer Ranch Holdings deducted nearly \$24 million in 2006 as the value.

The IRS challenged the number of units that could be built on the parcel. The Tax Court reduced the deduction to slightly less than \$20 million. The appeals court remanded the case for the Tax Court, which adopted the donor's valuation. The IRS then argued that the valuation should be adjusted to account for the declining real estate market. The IRS, which was told it would need to provide comparable sales as evidence of a declining market, "failed to quantify the amount" by which its expert accounted for the softening real estate market, said the Tax Court. Because it had no basis to compute an adjustment, the court agreed with the donor (*Palmer Ranch Holdings Ltd., v. Comm'r.*, T.C. Memo. 2016-190).

PHILANTHROPY PUZZLER

Lynda and Jerry established a charitable remainder unitrust in April 2016. The charity sent the couple a charitable deduction computation based on the use of February's 2.2% §7520 rate. This rate gave them a larger charitable deduction than would the use of April's 1.8% rate. Lynda and Jerry have kept the computation and plan to include a copy when they file their 2016 income tax return. They have asked if they need any other documentation.

CHANGES IN TAX NUMBERS

A new year means new tax numbers, thanks to inflation adjustments (Rev. Proc. 2016-55). Among the changes taking effect in 2017:

	2016	2017
Gift, generation-skipping transfer and estate tax exclusion	\$5,450,000	\$5,490,000

	2016	2017		2016	2017
IRA contribution limit	\$5,500	\$5,500	Joint	\$466,950	\$470,700
Personal and dependent exemption	4,050	4,050	Head of household	441,000	444,550
Standard deduction			Married filing separately	233,475	235,350
Single	6,300	6,350	Alternative minimum tax exemptions		
Joint	12,600	12,700	Single, head of household	53,900	54,300
Head of household	9,300	9,350	Joint	83,800	84,500
Married filing separately	6,300	6,350	Married filing separately	41,900	42,250
Cutbacks on itemized deductions and personal exemptions begin			Kiddie tax	2,100	2,100
Single	259,400	261,500	Nanny tax	2,000	2,100
Joint	311,300	313,800	Annual gift tax exclusion	14,000	14,000
Head of household	285,350	287,650	Annual gift tax exclusion for non-citizen spouse	148,000	149,000
Married filing separately	155,650	156,900	Special use valuation for real property devoted to farming or closely held business use	1,110,000	1,120,000
Tax brackets			401(k) contribution limit	18,000	18,000
25% bracket starts			401(k) catch-up contribution limit	6,000	6,000
Single	37,650	37,950	Savings bond interest exclusion phased out		
Joint	75,300	75,900	Single, head of household	92,550	93,150
Head of household	50,400	50,800	Joint	146,300	147,250
Married filing separately	37,650	37,950			
28% bracket starts					
Single	91,150	91,900			
Joint	151,900	153,100			
Head of household	130,150	131,200			
Married filing separately	75,950	76,550			
33% bracket starts					
Single	190,150	191,650			
Joint	231,450	233,350			
Head of household	210,800	212,500			
Married filing separately	115,725	116,675			
35% bracket starts					
Single, joint, head of household	413,350	416,700			
Married filing separately	206,675	208,350			
39.6% bracket starts					
Single	415,050	418,400			

PUZZLER SOLUTION

Split-interest charitable gifts may be valued using the §7520 rate for the month of the gift or either of the two prior months, whichever is most favorable [Code §7520(a)]. If Lynda and Jerry plan to use the rate for February rather than April, they must attach a statement to the return on which the deduction is claimed. They must state that an election is being made under Code §7520(a) to use a rate for a month other than the month of the gift, describe the interest being valued, provide the applicable valuation rate absent the election and inform the IRS of the month and rate chosen to value the gift [Reg. §1.7520-2(b)].

FACTS, FIGURES, SURVEYS AND STATS

How and why Americans give and to which organizations is the focus of numerous studies. Among the findings from various sources:

■ The IRS reports, in its most recent Statistics of Income Bulletin, that 11,917 estate tax returns were filed in 2015, for decedents dying in 2014 and 2015. Of these, 4,918 were taxable estates. There were 2,632 estates, with a combined net worth of about \$60.9 billion, on which charitable deductions were claimed. The total value of the charitable bequests was \$20,385,803. California accounted for the most of any state, with 370 of those estates and with gifts totaling \$3,748,429.

■ The National Philanthropic Trust's 2016 Donor Advised Fund Report shows a total of \$78.64 billion held in more than 269,000 donor advised funds, a 12% increase over the previous year. Of the 1,000 funds tracked, Fidelity Investments Charitable Gift Fund made the most grants in both 2013 and 2014 at nearly \$1.8 billion and more than \$2.2 billion respectively. The total of all grants from donor advised funds was more than \$14.5 billion. Meanwhile, new contributions to the funds were \$22.26 billion. The average donor advised fund account was \$235,727.

■ The top five issues of interest to young philanthropists were animal welfare, hunger, homelessness, the environment and the economy, according to a 2012 DoSomething.org index on young people and volunteering.

■ Total charitable giving in the U.S. is estimated at \$373.25 billion in 2015, according to *Giving USA 2016*, a publication by Giving USA Foundation. This was a 4% inflation-adjusted increase. The largest portion (82%) of that came from individuals, at \$264.58 billion (up 3.7%). Foundation gifts accounted for \$58.46 billion, while corporations

gave \$18.45 billion. The largest share of the gifts went to religious organizations, at \$119.3 billion.

■ The Health and Retirement Study, funded by the National Institute on Aging and administered by the Population Research Center at the University of Michigan, found that the share of U.S. adults ages 55 and older with wills or trusts has been declining since 2000. Among those with wills and trusts, the percentage including a charitable bequest has been increasing, primarily among those in the 55-64 and 65-74 age groups. The lack of wills and trusts may not mean that fewer individuals are leaving gifts at death, but rather that donors are relying more on non-probate methods, such as beneficiary designations and payable on death transfers.

■ The amount given to charity by single women has remained roughly the same between the early 1970s and today, according to Women Give 2016, a survey by the Women's Philanthropy Institute of the Indiana University Lilly Family School of Philanthropy. Pre-Boomer single women (those born before 1946) gave an average of about \$216, in today's terms. GenX and Millennial single women (those born in 1981 and later) are giving \$244, on average. Among married couples, pre-Boomer young women influenced charitable giving decisions 73% of the time, while among GenX and Millennials, young women had influence over 83.7% of gifts.

■ U.S. Trust's 2016 Study of High Net Worth Philanthropy found that 91% of high net worth households – those with net worth of at least \$1 million and/or annual household income of at least \$200,000 – gave to charity in 2015. This compares with 58.8% of the general population that gave in 2012, the most recent year for which figures are available.

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