Impact of the Revenue Reconciliation Act of 1993
on
Charitable Giving

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I. Introduction

A. This is intended to be only a survey of five selected aspects of the impact of the Revenue Reconciliation Act of 1993 upon charitable giving.

B. HPD will discuss, in order, the following new rules under RRA'93:

1. The rate structure.

2. The substantiation-of-gifts requirements.

3. The quid-pro-quo rules.

4. The alternative minimum tax rules for gifts of appreciated property.

5. The rules for deductions of lobbying expenses.

C. Questions and interruptions are welcome during the course of HPD's talk.

II. Rate structure

A. Income tax rates for individuals now reach up to 39.3% (or even higher if certain collateral consequences of other provisions are taken into effect).

1. The top tax bracket for ordinary income of individuals is now 36%. It applies for taxable income in excess of $140,000 for married individuals filing jointly and for surviving spouses. The other thresholds are:

a. $127,500 for heads of household.

b. $115,000 for single individuals.

c. $70,000 for married individuals filing separately.

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d. $5,500 for trusts and estates.

2. There is a 10% surcharge on top of that, bringing the top bracket to 39.3%, for taxable incomes over $250,000 for married individuals filing jointly, for surviving spouses, for heads of household, and for single individuals. The other thresholds are:

a. $125,000 for married individuals filing separately.

b. $7,500 for trusts and estates.

3. Net capital gains are subject, however, to a maximum rate of 28%.

B. The estate and gift tax rates now reach up to 55% (for taxable transfers over $3 million). There is a phase-out of the lower graduated rates and the unified credit for estates over $10 million. Those "benefits" are completely phased out for estates of $21,040,000 or more.

C. The generation-skipping transfer tax rate is 55%.

D. Because the deduction for charitable gifts reduces tax at the highest marginal rates applicable to the donor, the marginal benefit to the highest-income donors is now higher than before RRA'93. See Gene Steuerle, Charitable Giving in 1993, 60 TAX NOTES 1283 (August 30, 1993); Valerie C. Robbins, Charitable Remainder Trusts Should Flourish With Increases in Tax Rates, 24 TAX ADVISER 505 (1993).

III. Substantiation

A. Gifts of $250 or more, whether in cash or property, and whether or not subject to any quid-pro-quo amount, must be "substantiated" in order to be deductible. Section 13172(a) of the Revenue Reconciliation Act of 1993 added 170(f)(8), effective for contributions made on or after January 1, 1994.

1. The threshold had been $750 in the House version of the legisla-

tion, but the Senate reduced it to $250, and the Conference Committee accepted the Senate's version.

2. In computing the threshold, separate payments generally are not to be aggregated. A footnote in the legislative history reads:

> "Separate payments generally will be treated as separate contributions and will not be aggregated for the purposes of applying the $250 threshold. In cases of contributions paid by withholding from wages, the deduction from each paycheck will be treated as a separate payment. However, . . . it is expected that the Secretary of the Treasury will issue anti-abuse rules to prevent avoidance of the substantiation requirement by writing multiple checks on the same date."

3. The legislative history makes clear that "[t]axpayers may not rely solely on a canceled check as substantiation for a donation" above the threshold amount.

B. Per a December 21, 1993, news release (IR-93-121), the IRS reminded charities of the new $250 substantiation requirement as well as of the new $75 quid-pro-quo requirement (to be discussed below). Copies of IR-93-121 are available as handouts. The IRS has also developed a new Publication 1771, "Charitable Contributions — Substantiation and Disclosure Requirements," which was mailed to more than 500,000 charities in December 1993. Copies of that Publication are also available as handouts.

C. The burden and risk are on the donor: the sanction is loss of the charitable contributions deduction, per 170(f)(8)(A). Per Publication 1771:

> "[t]he responsibility for obtaining this substantiation lies with the donor, who must request it from the charity. The charity is not required to record or report this information to the IRS on behalf of donors."

D. The substantiation must be "contemporaneous" with the gift. The statute (170(f)(8)(C)) confirms, however, that this only means that the acknowledgment be received in time to be filed with the donor's tax return. Thus, if a donor gives $500 to a charity on Jan. 6, 1994, the Code defines "contemporaneous" to mean not later than April 15, 1995!

E. Per 170(f)(8)(B), the acknowledgment must contain:

1. The amount of cash and a description (but not value) of any property other than cash contributed.
2. Whether the donee organization provided any goods or services in consideration, in whole or in part, for the contribution.
3. A description and good faith estimate of the value of any goods or services referred to or, if such goods or services consist solely of intangible religious benefits, a statement to that effect.

F. The legislation provides that the substantiation requirement will not apply if the charity reports directly to the IRS the information required by the Code. This, however, will only be possible under regulations to be issued by the Treasury, and none have yet been proposed or issued. The legislative history indicates that these regulations should "clarify the treatment of contributions made through payroll deductions." It is not clear how donors will be informed of and allowed to rely on any such direct reporting procedure.

G. The legislation provides no particular format for the acknowledgment. Publication 1771 provides as follows:

> "For example, letters, postcards or computer-generated forms may be acceptable. The acknowledgement does not have to include the donor's social security or tax identification number. It must, however, provide sufficient information to substantiate the

> amount of the deductible contribution. The acknowledgement should note the amount of any cash contribution. However, if the donation is in the form of property, then the acknowledgement must describe, but need not value, such property. Valuation of the donated property is the responsibility of the donor."

H. Although the risk and burden is on the donor, the legislative history contains an important warning, saying it —

> "is intended that a charitable organization that knowingly provides a false written substantiation to a donor may be subject to the penalties provided for by section 6701 for aiding and abetting an understatement of tax liability."

Publication 1771 repeats this.

I. Despite the adoption of 170(f)(8), all other pre-RRA'93 substantiation requirements remain in effect, e.g., the need for an appraisal for gifts of property with a value in excess of $5,000 per 1.170A-13. Publication 1771 so states.

J. For further reading, see: Richard B. Ruge & Richard A. Speizman, Substantiation and Disclosure of Charitable Contributions: Congress Asks for More, 61 TAX NOTES 609 (Nov. 1, 1993); Richard Blumenreich, Refunds May Be Available for Clients Who Did Not Literally Follow the Substantiation Requirements for Certain Charitable Contributions of Property, 24 TAX ADVISER 356 (June 1993); Laura Kalick & Janet Buehler, Charitable Contributions: Substantiation and Valuation Requirements, 20 TAX ADVISER 242 (April 1989); Rochelle Korman, Selected Issues in Valuing and Substantiating Charitable Gifts of Property, 16 N.Y.U. CONF. ON TAX PLAN. CHARITABLE SECTOR 1-1 (1988); James K. Hasson, Jr., Appraisal and Substantiation Requirements for "In-kind" Contributions: A Summary of the Complex Temporary Regulations Issued Following DEFRA, 15 N.Y.U.

CONF. ON TAX PLAN. CHARITABLE SECTOR 9-1 (1987); James K. Hasson, Jr., Satisfying the Substantiation Requirements for Year-end Charitable Gifts, 63 J. TAX'N 388 (1985); Jacquin D. Bierman, Revenue Service Issues New Rules on Substantiating Charitable Gifts, 62 J. TAX'N 186 (1985); James E. Merritt & Tony M. Edwards, DRA Changes Affecting Charitable Contributions, Estate and Gift Tax Valuations and Appraisers, 16 TAX ADVISER 140 (1985).

IV. Quid Pro Quo

A. A charitable contribution deduction is allowed, in the words of the Code, only for "a gift or contribution." Neither the Code nor the Regulations provide any guidance about how to interpret those words. The courts have tended to take somewhat different approaches depending on which of the two words — "gift" or "contribution" — they interpret:

1. The leading case on the definition of a "gift," not for purposes of 170 but for purposes of 102 (excluding gifts from the income of the donee), is Commissioner v. Duberstein, 363 U.S. 278, 286 (1960), which defined it as a transfer proceeding from "detached and disinterested generosity." This focusses on the state of mind of the donor. The Duberstein verbal formula has often been used by other courts in interpreting 170. E.g., DeJong v. Commissioner, 309 F.2d 373 (9th Cir. 1962).

2. The courts have interpreted "contribution" in a somewhat different manner, focussing not on the state of mind of the donor but upon the more objective criterion of whether anything of value was received back by the donor. The Supreme Court has said:

"A payment of money generally cannot constitute a charita-

> ble contribution if the contributor expects a substantial benefit in return. . . . The *sine qua non* of a charitable contribution is a transfer of money or property without adequate consideration." United States v. American Bar Endowment, 477 U.S. 105, 116, 118 (1986).

Under either formulation, no deduction would be available for transfers of money or property to an eligible charitable donee if the transferor received, in exchange, services or property of equal value — a "quid pro quo." Thus, for example, no parent gets 170 deductions for paying for a child to attend the N.Y.U. School of Law. Rev. Rul. 83-104, 1983-2 C.B. 46, superseding Rev. Rul. 79-99, 1979-1 C.B. 108.

B. The transferor has the burden of proof on the question of whether the transfer was a "gift or contribution." The IRS and the courts have tended to enforce that rule. Indeed, the IRS frequently asserts that there is a *presumption* that, if *any* quid pro quo is received, *no* deductible gift has been made. Thus, if the transferor receives any benefit in return for the transfer, there will be no deduction available unless the transferor establishes both (1) the value of the benefit received and (2) that the excess transferred was a "gift or contribution." The IRS has long ruled, however, that if the transferor carries that burden, a charitable contribution deduction will be allowed for the excess of the amount transferred over the quid pro quo. E.g., Rev. Rul. 67-246, 1967-2 C.B. 104.

C. For years, concern has been rising that there was no effective administrative enforcement mechanism to deal with quid-pro-quo gifts. The transferors had economic incentives to distort, minimize, or ignore the value of the quid pro quo; the donees had no requirement to disclose, much less firmly fix, its value. A few historical signposts, chosen by HPD, are worth recalling:

1. Some members of the A.B.A. Tax Section met with the Service in May of 1988, and later submitted a series of questions and answers — drafted by them — dealing with quid-pro-quo concerns. Among the A.B.A. comments were:

> "[T]he transferee charity is under a duty neither to misrepresent the value of the contribution nor to misstate the legal consequences of the payment or transfer in question. For example, where the fundraising activity is designed to solicit payments which are intended to be in part gifts and in part the purchase of admissions, the charity should make clear not only that part of each payment represents payment for a non-deductible admission charge, but also the amount which is in fact deductible as a gift. The amounts properly attributable to each part of the payment should be determined in advance of the solicitation, should be stated in making the solicitation, and clearly indicated on any ticket, receipt or other evidence issued in connection with the payment."

And, further:

> "Q12: In the case of a payment or transfer to a charitable organization where all or a portion of such transfer or payment may not be deductible as a charitable contribution, is it appropriate for the charitable transferee, in soliciting the payment or acknowledging receipt, to make a statement to the effect that 'our organization is a charitable organization, contributions to which are deductible for federal income tax purposes to the full extent permitted by law'?
>
> "A12: A solicitation or acknowledgment of a payment which uses the language suggested above, although not a blatant misstatement of law, could under certain circumstances be construed as unnecessarily misleading. The use of language similar to that suggested above does nothing to establish a presumption in favor of a deduction of any kind, and may, in the future, be treated by auditing agents as a rea-

son for subjecting contribution deductions to closer scrutiny than has been true in the past."

2. Despite the growing concerns, there was some indication that tax-exempt organizations themselves had no legally-enforceable duty to disclose the value of quid-pro-quo payments. For example, in Technical Advice Memorandum 8832003 (May 6, 1988), the IRS discussed a tax-exempt organization which sponsored educational exchange travel programs. Participants were encouraged to bring "companions." The brochures stated that the organization was tax-exempt under 501(c)(3) and that:

> "40% of the above price is considered a charitable contribution to further its purposes. This applies to spouses as well. The remainder of the fee paid by the professional, however, is deductible under section 162 and/or 274."

The ruling first held that the organization had made "a good faith effort to comply" with Rev. Rul. 67-246. It went on, however, to state (in dictum):

> "[N]either the Internal Revenue Code nor other legal precedent have evolved to the point where sanctions would be imposed on a section 501(c)(3) organization for noncompliance with Rev. Rul. 67-246 or providing incorrect information as to what portion of member contributions or other fees are deductible under section 170."

3. In response to Congressional pressure, and in recognition of the importance of the problem, the IRS issued Publication 1391 in August 1988, and distributed it widely to 501(c)(3) organizations. It reprinted Rev. Rul. 67-246, and also contained a message from then-Commissioner Larry Gibbs, which read in part as follows:

> "Because of this expression of Congressional interest, as

> well as the continued concern of IRS, I shall institute a Special Emphasis Program for the 1988 tax year. It will focus on the fund-raising practices of charitable organizations, as well as organizations that perform fund-raising functions for charities. Through this Special Emphasis Program, the IRS shall seek to ascertain the extent to which taxpayers are furnished accurate and sufficient information concerning the deductibility of their contributions."

4. In December of 1988, the Service issued Technical Advice Memorandum 8909004 (December 2, 1988). It referred to TAM 8832003 (the earlier precedent), and directed that further audit activities proceed to determine whether the organization truly "operated exclusively for educational purposes." This second memo, however, did not directly cast any doubt on the above-quoted no-sanctions statement.

5. By early 1990, the Service was clearly changing its tune. Technical Advice Memorandum 9027003 (March 21, 1990), like the earlier ones, involved a tax-exempt organization which conducted educational tours. The brochures in this case indicated that, in addition to the quoted price for the tour, a "gift" to the organization would be due prior to departure. It referred to that "gift" as "tax deductible." The Service first concluded that, on the facts, the "gift" was "not a freely given contribution but, rather, a payment to entitle one to go on a tour." The memorandum then proceeded to address the question of possible sanctions to the organization. The two relevant paragraphs are quoted, in full:

> "Under the Tax Equity and Fiscal Responsibility Act of 1982, provisions were made for the assertion of new penalties in the area of tax abuse. These provisions are not limited to

tax shelter situations, but could be applicable in other situations. Section 6700 is the abusive tax shelter penalty provision. It could apply where an exempt organization assisted in an arrangement and furnished a statement to secure tax benefits knowing the benefits to be fraudulent. Section 6701 is the aiding and abetting provision. The penalty here would apply if an exempt organization aided or assisted in the propagation or presentation of any portion of a return, affidavit, claim or other document, knowing it would be used in connection with an Internal Revenue law matter, and knows that if used, it will result in an understatement of tax liability.

"We are concerned about misrepresentations to the public about tax deductible contributions or gifts. In a situation where an exempt organization knowingly continued to represent that amounts paid or contributed to it would entitle an individual to a deduction on his or her income tax return when in fact no deduction would be permitted, the provisions of either section 6700 or 6701 of the Code could come into play. Where an individual obtains a travel tour as part of a quid pro quo exchange, there would be no charitable deduction. Continued misrepresentations about these matters raise the possibility that the penalty provisions could come into play. Moreover, continued misrepresentations regarding tax matters could raise questions as to whether public purposes are still being served by continued exemption. Finally, [the subject organization] is hereby placed on notice that it should modify its travel tour solicitation program, preferably as previously discussed, to remove such misrepresentations."

The next-to-last sentence clearly threatens loss of tax exemption. The penalty risks under 6700 and 6701 are also worth noting.

6. By the end of 1990, the situation was unmistakably clear. In his outline for the P.L.I. Program on "Nonprofit Organizations 1990," Howard M. Schoenfeld, Special Assistant for EO Matters at the IRS,

discussing this issue, listed several "sanctions available to IRS to enforce compliance in this area," and specifically included "revocation of tax-exempt status." Schoenfeld, Current Compliance Concerns of the IRS, NONPROFIT ORGANIZATIONS 1990 — CURRENT ISSUES AND DEVELOPMENTS 367, at 377 (P.L.I. Coursebook 307, J4-3644, 1990).

7. Nevertheless, Congress and the Service continued to be concerned at abuses, and worried about the lack of administrative means to uncover abuses. Legislation passed Congress in 1992 which would have required donees to disclose and value quid-pro-quo payments, but it was vetoed by the President.

8. Finally, as part of RRA'93, two new provisions were added to the Code: new 6115 requires charities to disclose, in writing, the existence and amount of any quid-pro-quo payment in connection with any transfer of more than $75;[1] new 6714 imposes penalties upon charities for failure to comply with the disclosure requirements. They are effective for quid-pro-quo contributions made after 1993.

D. Let's explore the provisions in more detail:

1. 6115(a) requires donees (described in 170(c), but not including governments, etc., described in 170(c)(1)) to make two types of written disclosure in connection with the solicitation or receipt of

1. Note that the $250 substantiation rules apply to gifts of $250 or more, whereas the quid-pro-quo rules apply to gifts of more than $75. Furthermore, an example in the legislative history makes clear that the more-than-$75 threshold applies to the gross amount of the donor's payment, not merely to the excess above the quid-pro-quo amount.

a quid-pro-quo contribution in excess of $75 —

a. A statement informing the donor that the deduction is limited to excess of what was transferred over the value of what was received back, i.e., a statement of law, and

b. A good-faith estimate of the value of what was received back, i.e., a statement of fact.

There is no precise time prescribed by the statute for delivering this writing, but the "contemporaneous" rule of 170(f)(8)(C) does not apply.

2. 6115(b) defines a "quid pro quo contribution" as:

> "a payment made partly as a contribution and partly in consideration for goods or services provided to the payor by the donee organization."

It goes on to provide a quite-interesting exception (to which we'll revert later):

> "A quid pro quo contribution does not include any payment made to an organization, organized exclusively for religious purposes, in return for which the taxpayer receives solely an intangible religious benefit that generally is not sold in a commercial transaction outside the donative context."

3. 6714(a) provides penalties. It reads as follows:

> "If an organization fails to meet the disclosure requirement of section 6115 with respect to a quid pro quo contribution, such organization shall pay a penalty of $10 for each contribution in respect of which the organization fails to make the required disclosure, except that the total penalty imposed by this subsection with respect to a particular fundraising event or mailing shall not exceed $5,000."

Given the prior history, in which *other* penalties (including perhaps even revocation of tax exemption) were threatened, should the enactment of 6714 be understood as supplanting these other sanctions and as being, now, the exclusive sanction for violations of this requirement? HPD's view is to the contrary.

4. 6714(b) provides a helpful exception to the 6714(a) sanctions: "No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause." There is no indication, in the legislative history or elsewhere, about what might constitute "reasonable cause." It may be that, for a short period of time, ignorance of the new rules might constitute such cause, but:
   a. This is a risky proposition,
   b. It certainly will not last very long, and
   c. Given the IRS's massive mailing of Publication 1771, it may not apply at all.

E. Although the statute does not prescribe any form or other requirements for the quid-pro-quo statements, the Senate Committee explanation says:

> "[I]t is intended that the disclosure be made in a manner that is reasonably likely to come to the attention of the donor. For example, a disclosure of the required information in small print set forth within a larger document might not meet the requirement."

This is picked up and repeated in Publication 1771.

F. Despite the statutory definition of a quid-pro-quo donation, and our common sense understanding of the notion, it is surprisingly hard to draw lines at the margins. We will consider three examples:

1. Suppose a charitable donee gives its donors a coffee mug, with its logo on it, whenever they contribute $100 or more? In Rev. Proc.

90-12, 1990-1 C.B. 471, the Service set guidelines for determining when such items have such "insubstantial fair market value" that they may be disregarded, i.e., so the donor can take a deduction for the full amount given to charity without any reduction for the value of the mug or similar item. The guidelines state that such items will be treated as having an "insubstantial fair market value" if either (a) the fair market value of the benefits is the lesser of \$50 or less than 2% of the amount of the gift, or (b) the "gift" is \$25 or more and the benefits are "token items" with a value of \$5 or less. These latter dollar amounts are subject to inflation adjustments. Rev. Proc. 90-12 was amplified by Rev. Proc. 92-49, 1992-1 C.B. 987. Both were discussed in the legislative history; both were relied on in the legislative history as setting forth guidelines for the type of quid-pro-quo benefit which will *not* trigger 6115 reporting; and both are explicitly referred to in Publication 1771 as fixing the limits for an exception from 6115. It is doubtful whether the IRS will authorize any further flexibility in testing for de minimis benefits beyond what is provided in those Revenue Procedures.

2. Suppose X gives C, a charity, \$100 and C gives X an item worth \$100? From one point of view, there is clearly a quid-pro-quo payment involved. The problem is that there appears to be no *donation or gift* involved. Is 6115 triggered? The legislative history says:

> "[T]he provision will not apply to transactions that have no donative element (e.g., sales of goods by a museum gift shop that are not, in part, donations)."

This exception, too, is repeated in Publication 1771.

3. Suppose X gives C, a church, $100 and receives in exchange religious instruction? This question brings us to the brink of a huge legal chasm, and opens some wonderful history for examination. HPD will be brief, but several steps need to be taken to answer the question:

   a. In Rev. Rul. 78-179, 1978-1 C.B. 68, the Service ruled that no deduction was available in such circumstances when the donor received, in exchange for the donation, "auditing" and personal counseling services.

   b. The ruling was evidently aimed at the Scientology churches. At that time, the IRS was conceding that they were, indeed, churches and entitled to tax exemption. It stipulated to that, but went on to challenge the deductibility of payments for such auditing and personal counseling services. In Hernandez v. Commissioner, 490 U.S. 680 (1989), the Supreme Court sustained the IRS's denial of deductions.

   c. Meanwhile, the IRS had changed its position, and directly attacked the tax-exempt status of Scientology organizations. It argued that they were *not* tax exempt because they permitted personal inurement (to the benefit of L. Ron Hubbard) and because they contravened fundamental public policy by violating the law. Here, again, the Service was sustained by the courts. E.g., Church of Scientology of California, 83 T.C. 381 (1984), aff'd on other grounds, 823 F.2d 1310 (9th Cir. 1987), cert. denied, 486 U.S. 1015

(1988).

d. Meanwhile, many — perhaps hundreds — of donors to Scientology were litigating their own deductions. The organization itself was engaged in massive ongoing litigation with the IRS. L. Ron Hubbard died. And, finally, on October 1, 1993, the Service and the Scientologists announced a settlement under which the Scientology organizations would be recognized, once more, as tax exempt. The details have not been revealed, but attorneys involved in the matter have hinted that this resulted from the cessation of private inurement (L. Ron Hubbard was, after all, dead) and an agreement to cease any further violations of law (the fundamental public policy issue).

e. Then, in November of 1993, the IRS surprised many observers by issuing Rev. Rul. 93-73, 1993-34 I.R.B. 7. It declared Rev. Rul. 78-179 obsolete. This flustered and confused many observers. On the one hand, there is often no substantive meaning to the IRS's action in declaring one of its prior precedents obsolete. On the other hand, however, it appeared that the Service might be giving up a position which it had litigated to and won in the Supreme Court. And, after all, that victory, in Hernandez, was based on the stipulation that Scientology was entitled to tax-exempt status.

f. Within the last months of 1993, the Church of Scientology provided its members with a booklet entitled, "Information on Taxes and Your Donations." It describes the settlement, restoring tax-exempt status to the Church. It goes on, however, to say, in part,

> "the [settlement] action means that donations you make to the Church — including donations for auditing and training — qualify as charitable contributions and can be claimed as deductions on your federal (and state) income tax returns!"[2]

g. There remains no good information available about the meaning of Rev. Rul. 93-73. It would be foolish to take it to signal any backing off by the IRS from its long-standing quid-pro-quo views. Until more facts are revealed, only confusion can reign. It would not be surprising if Congressional hearings were eventually held on this subject.

So, in light of this history, what's the answer to our question? There are two perspectives from which the question might be understood: from the perspective of the donor or that of the donee. As to the former, we will need further illumination to decide whether the donor is entitled to a deduction in this and many somewhat analogous religious situations.[3] As to the latter, however, Congress has spoken. It has made clear that, for purposes of the 6115 quid-pro-quo disclosures, an "intangible religious benefit"

2. As quoted in the January 3, 1994, edition of TAX NOTES TODAY.

3. It is clear, from a footnote in the legislative history, that neither 6115 nor 6714 are intended in any way to affect the answer to this question under pre-RRA'93 law.

will not count.[4] Thus, the donee does not have to comply with 6115, and is not subject to 6714 penalties for failing to do so. This is reflected in Publication 1771, which elaborates as follows:

> "An example of an intangible religious benefit would be admission to a religious ceremony. The exception also generally applies to de minimis tangible benefits, such as wine, provided in connection with a religious ceremony. The intangible religious benefit exception, however, does not apply to such items as payments for tuition for education leading to a recognized degree, or for travel services, or consumer goods."

Interestingly, although disclosure of intangible religious benefits is not required under the quid-pro-quo rules, it *is* required under the $250 substantiation rules! Publication 1771, picking up on some language in the legislative history, says:

> "If the goods or services consist entirely of intangible religious benefits, the statement should indicate this, but the statement need not describe or provide an estimate of the value of these benefits."

G. Many open questions will need to be resolved before we fully understand the scope of the quid-pro-quo disclosure rules. For example, suppose X gives $1,000 to N law school. Six months later, as has been N's practice for years, N gives an annual recognition dinner to which it invites many alumni, faculty, and donors, including X. X is not charged for the dinner. Is the dinner a quid pro quo? Must N so state in writing to X? Must X reduce his deduction by the value of the dinner? The problem here is part of a generic set of practices in which donors are recognized, but the nexus of the recognition to the donation is weak,

4. For the precise language of 6115(b), see ¶ IV.D.2 at p. 13 above.

chronologically or otherwise. HPD hopes that some common sense flexibility is built into the ultimate regulations under 6115. It will be helpful here if concerned donees consider the issue carefully, and write their comments to the Treasury. If anyone does this, please be sure to consider the issue carefully from both sides; it will be counter-productive to suggest a "solution" which, as reasonably perceived by the Treasury folks, would open up big loopholes or gut the purpose of 6115.

H. For further reading on this subject, see: Thomas Silk & Robert A. Wexler, How to Reach Fundraising Goals After RRA '93, 5 TAX'N EXEMPT ORG'S 147 (1994); Helleloid, Strong & Weber, Deduction of Charitable Contributions with Personal Benefits Remains Uncertain, 73 J. TAX'N 210-19 (Oct. 1990); Note, *Hernandez v. Commissioner*, 43 TAX LAW. 491-501 (Winter 1990); Note, A Line Drawn by Unsteady Hands: Section 170, Charitable Contributions, and Return Benefits in *Hernandez v. C.I.R.*, 23 AKRON L. REV. 575-85 (Spring 1990); Anno., 88 A.L.R. FED. 398 (1990); Scott N. Cairns, Diane A. Riordan & Michael P. Riordan, The Deductibility of Charitable Contributions After Rev. Proc. 90-12: New Guidelines for Charitable Organizations, 21 TAX ADVISER 643 (1990); DAVID M. DONALDSON & CAROLYN M. OSTEEN, A MANUAL ON THE TAX ASPECTS OF CHARITABLE GIVING 106-11 (1st ed. 1992); BARBARA L. KIRSCHTEN & CARLA A. NEELEY, CHARITABLE CONTRIBUTIONS: INCOME TAX ASPECTS A-18 - 31 (BNA Tax Mgmt. Portfolio 521, 1991).

V. AMT (Appreciated Property Gifts)

A. The history of the treatment of charitable gifts of appreciated property is twisted.

1. Prior to 1987, with exceptions not here relevant, individuals could generally deduct the fair market value of property donated to charities, even if their basis in the property was less than fair market value.

2. Section 701 of the Tax Reform Act of 1986 added 57(a)(6) to the Code, broadening the definition of "tax preference" item to include the appreciation in value of capital gain property. The provision was effective beginning in 1987. This made such appreciation in value subject to the alternative minimum tax provisions of the Code.

3. An exception was later made for contributions of tangible personal property in taxable years beginning in 1991. Pub. L. No. 101-508, § 11344. Thus, donations of such property in 1991 were *not* subject to the AMT. Of course, donations of any *other* appreciated property — e.g., real estate or intangible property — remained subject to the AMT.

4. A further exception was later made for contributions of tangible personal property made before July 1, 1992, in taxable years beginning in 1992. Pub. L. No. 102-227, § 112.

5. As of July 1, 1992, the exceptions ceased to apply, and the original "tax preference" item definition, which included tangible personal property, was again in effect. Thus, once again, donations of all such appreciated property became subject to the AMT.

That was the status of the law as of the summer of 1993. Of course, as we shall see in a moment, RRA'93 changed this dramatically.

B. The tax policy issue is fairly clear: it is difficult to justify granting a deduction for that portion of the value of a charitable gift which has never been included in the income of (and thus has never become part of the basis of the property in the hands of) the donor. As stated by one of the leading scholars in the field:

> "Whatever its origin, the fair market value rule must now be viewed as a subsidy or artificial inducement, above and beyond mere tax exemption, for philanthropic giving. The magnitude of the subsidy is a function of the amount of unrealized appreciation in relation to the basis of the property and the taxpayer's rates of tax, being greatest for taxpayers in highest brackets and with most appreciation. For a taxpayer in the top rate brackets whose property has a nominal basis, the rule operates in a sense to make the Government take over the whole cost of a charitable donation." William D. Andrews, Personal Deductions in an Ideal Income Tax, 86 HARV. L. REV. 309, 372 (1972) (footnotes omitted).

Nevertheless, the fair-market-value deduction has become well entrenched in the Code (subject to certain exceptions, e.g., for ordinary-income and short-term-capital-gain property). The AMT was the only recent broad-based attempt to mitigate the rule.

C. The AMT was quite widely misunderstood. It may help to set forth two truths about the AMT, as stated by leading commentators:

1. "While [the Code] subjects the appreciation to the alternative minimum tax, . . . a gift will never increase the donor's tax bill." DAVID M. DONALDSON & CAROLYN M. OSTEEN, A MANUAL ON THE TAX ASPECTS OF CHARITABLE GIVING 315 (1st ed. 1992).

2. "[E]ven in a worst case scenario, a gift of appreciated property will

result in a tax savings . . . ." DAVID M. DONALDSON & CAROLYN M. OSTEEN, A MANUAL ON THE TAX ASPECTS OF CHARITABLE GIVING 318 (1st ed. 1992).

D. Despite these tax policy and technical tax points, there was a perception that the AMT chilled charitable giving. (It may have been more accurate to observe that a *temporary* AMT would chill charitable giving. Discuss.) Under the strong leadership of Sen. Moynihan, Congress repealed the AMT on appreciated property altogether in RRA'93.

E. The House version of RRA'93 contained two provisions, one dealing the AMT for individuals and the other with the AMT for corporations. Both were accepted by the Senate and the Conference Committee and were enacted.

1. As to individuals, the Act eliminates the treatment of contributions of appreciated property (real, personal, and intangible) as a tax preference for AMT purposes. Section 13171(a) of RRA'93 repealed 57(a)(6) altogether, restoring the law to its pre-TRA'86 state. The amendment is effective retroactively as follows: (a) in the case of contributions of tangible personal property, for contributions made after June 30, 1992, and (b) in all other cases, for contributions made after 1992.

2. As to corporations, RRA'93 provides that no adjustment related to the earnings and profits effects of any charitable contribution shall be made in computing the ACE component of the corporate AMT. The relevant pre-RRA'93 provisions of 56(g)(4), dealing with "adjusted current earnings," were also repealed, by § 13171(b) of RRA'93, which added 56(g)(4)(J). The retroactive effective date

provision is the same as for the repeal of 57(a)(6) for individuals (see ¶ V.E.1 at p. 23 above).

F. Congress also asked the Treasury to prepare a report to Congress on an advance valuation procedure for charitable gifts. The House had made this part of the legislation; the Senate deleted that provision; the Conference Committee indicated in the legislative history, but not in the statutory language, that the report should be prepared. In the language of the legislative history, the report should discuss:

> "the development of an advance valuation procedure under which a taxpayer could elect to enter into an agreement with the Secretary regarding the value of tangible personal property prior to the donation of such property to a qualifying charitable organization (provided that time limits for donation and any other conditions contained in the agreement are satisfied). The report should address the advisability of establishing threshold amounts for claimed value and imposing user fees as prerequisites for seeking an agreement under the procedure, possible limitations on applying the procedure only to items with significant artistic or cultural value, and recommendations for legislative action needed to implement the procedure."

G. For further reading, see: Mara J. Lozier, New Incentives to Give: Impacts of the 1990 Amendment to Section 57 on Charitable Contributions of Appreciated Tangible Property, 44 TAX LAW. 885 (1991); Robin Hartzog, AMT and Charitable Contributions of Appreciated Property, 21 TAX ADVISER 761 (1990); DAVID M. DONALDSON & CAROLYN M. OSTEEN, A MANUAL ON THE TAX ASPECTS OF CHARITABLE GIVING 315-23 (1st ed. 1992).

VI. Lobbying Activities

A. RRA'93 generally disallows deductions for certain types of lobbying expenses. These rules generally apply to for-profit entities (per 162(e)) and to dues paid to nonprofits *other than 501(c)(3)'s* (per 162(e)(3)). The associated reporting requirements (of 6033(e)) also do not apply to 501(c)(3)'s, per 6033(e)(1)(B)(i).

B. 501(c)(3)'s need to be aware of the new rules, however, for a limited purpose: 170(f)(9) — dealing with charitable contribution deductions for certain donations used to support lobbying — prevents an end-run around 162(e).

1. The Conference Committee Report describes 170(f)(9) as:

> "an anti-avoidance rule designed to prevent donors from using charities as a conduit to conduct lobbying activities, the costs of which would be nondeductible if conducted directly by the donor."

2. 170(f)(9) disallows deductions under 170 or 162 for contributions or payments to a 501(c)(3) organization which conducts lobbying activities as described in 162(e)(1) if:

   a. the lobbying activities in question are "of direct financial interest to the donor's trade or business," and

   b. "a principal purpose of the contribution was to avoid Federal income tax by securing a deduction for such activities under this section which would be disallowed by reason of section 162(e) if the donor had conducted such activities directly."

3. The Conference Committee Report says that the determination whether the "principal purpose" test is met should —

"be based on the facts and circumstances surrounding the contribution, including the existence of any formal or informal instructions relating to the charity's use of the contribution for lobbying efforts (including nonpartisan analysis), the temporal nexus between the making of the contribution and the conduct of the lobbying activities, and any historical pattern of contributions by the donor to the charity."

Tax Notes Today
DECEMBER 22, 1993 WEDNESDAY
IRS OUTLINES NEW RULES
AFFECTING CHARITABLE ORGANIZATIONS
(IR-93-121)
SUMMARY

The Service in a news release (IR-93-121) has reminded charitable organizations that, because of changes made by OBRA '93, there's a new substantiation requirement for certain contributions received after December 31, 1993.

Beginning January 1, 1994, the Service says, charities receiving "quid pro quo contributions" in excess of $75 must provide a written statement to the donor. A quid pro quo contribution is one in which part of the payment is for goods or services received and part is a contribution.

The statement must contain a good-faith estimate of the value of the goods and services, and it must inform the donor that the charitable deduction is limited to the amount of the payment in excess of the value of the goods and services provided. The Service advises charities that they must provide the statement in connection with either the solicitation or the receipt of the contribution. A penalty of $10 per contribution can be imposed for each failure to provide the required statement. However, a written statement isn't required if the goods or services provided by the organization are de minimis token goods or services or an intangible religious benefit.

In the news release, the Service also outlines an OBRA '93 change affecting contributors. For charitable contributions of $250 or more made after December 31, 1993, the donor isn't allowed a deduction unless the gift is acknowledged by the charity in writing. Also, the donor must obtain the acknowledgment by the earlier of the date the return is filed or the due date of the return, including any extensions.

The acknowledgment must contain the amount of the cash or check and a description of the noncash property contributed. It must state whether the charity provided any goods or services in return for the contribution. If so, it must also include a description and good-faith estimate of the value of the goods or services or, if the goods and services consist solely of intangible religious benefits, a statement to that effect.

To help charities comply with the new rules, the Service has developed a new Publication 1771, "Charitable Contributions — Substantiation and Disclosure Requirements," which is being mailed this month to more than 500,000 charities. A copy of Pub. 1771 is attached to IR-93-121.

TEXT

NEW TAX LAW CHANGES AFFECT CHARITIES

Washington — Charities have a new substantiation requirement for certain contributions they receive on or after January 1, 1994, due to the Omnibus Budget Reconciliation Act of 1993.

To assist charities in complying with these new rules the IRS has developed new Publication 1771, Charitable Contributions — Substantiation and Disclosure Requirements. The IRS said it is mailing this publication to over 500,000 charities in December 1993.

Beginning January 1, charities receiving payments described as "quid pro quo contributions," in excess of $75, must provide a written statement to the donor. A quid pro quo contribution is one in which part of the payment is for goods or services received and part is a contribution.

This statement must give a good faith estimate of the value of the goods and services plus inform the donor that the charitable deduction is limited to the amount of the payment in excess of the value of the goods and services provided. For example, if a person gives a charity $100 and receives in exchange a $40 dinner, the charity must inform the donor in writing that the dinner was valued at $40 and only the portion of the payment exceeding the value of the dinner, $60, qualifies as a charitable contribution.

A written statement is not required if the goods or services provided by the organization are de minimis, token goods or services, or an intangible religious benefit.

The responsibility for providing disclosure statements for quid pro quo contributions over $75 rests with the charity. The charity must provide the statement in connection with either the solicitation or the receipt of the contribution. A penalty of $10 per contribution can be imposed on the charity for each failure to provide the required statement.

Charities also need to be aware of a new change affecting contributors. For charitable contributions of $250 or more made after Dec. 31, 1993, the donor is not allowed a deduction unless the gift is acknowledged by the charity in writing. Also, the donor must obtain the acknowledgement by the earlier of the date the return is filed or the due date of the return, including any extensions.

The acknowledgement must contain the amount of the cash or check and a description of any noncash property contributed. It must state whether the charity provided any goods or services in return for the contribution. If so, it must also include a description and good faith estimate of the value of the goods or services or, if the goods and services consist solely of intangible religious benefits, a statement to that effect.

A copy of Publication 1771 is attached.

Department of the Treasury
Internal Revenue Service
Publication 1771

Charitable Contributions — Substantiation and Disclosure Requirements

UNDER THE NEW LAW, CHARITIES WILL NEED TO PROVIDE NEW KINDS OF INFORMATION TO DONORS. Failure to do so may result in denial of deductions to donors and the imposition of penalties on charities.

Legislation signed into law by the President on August 10, 1993, contains a number of significant provisions affecting tax-exempt charitable organizations described in section 501(c)(3) of the Internal Revenue Code. These provisions include: (1) new substantiation requirements for donors, and (2) new public disclosure requirements for charities (with potential penalties for failing to comply). Additionally, charities should note that donors could be penalized by loss of the deduction if they fail to substantiate. THE SUBSTANTIATION AND DISCLOSURE PROVISIONS APPLY TO CONTRIBUTIONS MADE AFTER DECEMBER 31, 1993.

Charities need to familiarize themselves with these tax law changes in order to bring themselves into compliance. This Publication alerts you to the new provisions affecting tax-exempt charitable organizations. Set forth below are brief descriptions of the new law's key provisions. The Internal Revenue Service plans to provide further guidance in the near future.

DONOR'S SUBSTANTIATION REQUIREMENTS

Documenting Certain Charitable Contributions. — Beginning January 1, 1994, no deduction will be allowed under section 170 of the Internal Revenue Code for any charitable contribution of $250 or more unless the donor has contemporaneous written substantiation from the charity. In cases where the charity has provided goods or services to the donor in exchange for making the contribution, this contemporaneous written acknowledgement must include a good faith estimate of the value of such goods or services. Thus, taxpayers may no longer rely solely on a cancelled check to substantiate a cash contribution of $250 or more.

The substantiation must be "contemporaneous." That is, it must be obtained by the donor no later than the date the donor actually files a return for the tax year in which the contribution was made. If the return is filed after the due date or extended due date, then the substantiation must have been obtained by the due date or extended due date.

The responsibility for obtaining this substantiation lies with the donor, who must request it from the charity. The charity is not required to record or report this information to the IRS on behalf of donors.

The legislation provides that substantiation will not be required if, in accordance with regulations prescribed by the Secretary, the charity reports directly to the IRS the information required to be provided in the written substantiation. At present, there are no regulations establishing procedures for direct reporting by charities to the IRS of charitable contributions made in 1994. Consequently, charities and donors should be prepared to provide/obtain the described substantiation for 1994 contributions of $250 or more.

There is no prescribed format for the written acknowledgement. For example, letters, postcards or computer-generated forms may be acceptable. The acknowledgement does not have to include the donor's social security or tax identification number. It must, however, provide sufficient information to substantiate the amount of the deductible contribution. The acknowledgement should note the amount of any cash contribution. However, if the donation is in the form of property, then the acknowledgement must describe, but need not value, such property. Valuation of the donated property is the responsibility of the donor.

The written substantiation should also note whether the donee organization provided any goods or services in consideration, in whole or in part, for the contribution and, if so, must provide a description and good-faith estimate of the value of the goods or services. In the new law these are referred to as "quid pro quo contributions."

Please note that there is a new law requiring charities to furnish disclosure statements to donors for such quid pro quo donations in excess of $75. This is addressed in the next section regarding Disclosure By Charity.

If the goods or services consist entirely of intangible religious benefits, the statement should indicate this, but the statement need not describe or provide an estimate of the value of these benefits. "Intangible religious benefits" are also discussed in the following section on Disclosure By Charity. If, on the other hand, the donor received nothing in return for the contribution, the written substantiation must so state.

The present law remains in effect that, generally, if the value of an item or group of like items exceeds $5,000, the donor must obtain a qualified appraisal and submit an appraisal summary with the return claiming the deduction.

The organization may either provide separate statements for each contribution of $250 or more from a taxpayer, or furnish periodic statements substantiating contributions of $250 or more.

Separate payments are regarded as independent contributions and are not aggregated for purposes of measuring the $250 threshold. However, the Service is authorized to establish anti-abuse rules to prevent avoidance of the substantiation requirement by taxpayers writing separate smaller checks on the same date.

If donations are made through payroll deductions, the deduction from each paycheck is regarded as a separate payment.

A charity that knowingly provides false written substantiation to a donor may be subject to the penalties for aiding and abetting an understatement of tax liability under section 6701 of the Code.

DISCLOSURE BY CHARITY
OF RECEIPT OF QUID PRO QUO CONTRIBUTIONS

Beginning January 1, 1994, under new section 6115 of the Internal Revenue Code, a charitable organization must provide a written disclosure statement to donors who make a payment, described as a "quid pro quo contribution," in excess of $75. This requirement is separate from the written substantiation required for deductibility purposes as discussed above. While, in certain circumstances, an organization may be able to meet both requirements with the same written document, an organization must be careful to satisfy the section 6115 written disclosure statement requirement in a timely manner because of the penalties involved.

A quid pro quo contribution is a payment made partly as a contribution and partly for goods or services provided to the donor by the charity. An example of a quid pro quo contribution is where the donor gives a charity $100 in consideration for a concert ticket valued at $40. In this example, $60 would be deductible. Because the donor's payment (quid pro quo contribution) exceeds $75, the disclosure statement must be furnished, even though the deductible amount does not exceed $75.

Separate payments of $75 or less made at different times of the year for separate fundraising events will not be aggregated for purposes of the $75 threshold. However, the Service is authorized to develop anti-abuse rules to prevent avoidance of this disclosure requirement in situations such as the writing of multiple checks for the same transaction.

The required written disclosure statement must:

(1) inform the donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of any money (and the value of any property other than money) contributed by the donor over the value of goods or services provided by the charity, and

(2) provide the donor with a good-faith estimate of the value of the goods or services that the donor received.

The charity must furnish the statement in connection with either the solicitation or the receipt of the quid pro quo contribution. If the disclosure statement is furnished in connection with a particular solicitation, it is not necessary for the organization to provide another statement when the associated contribution is actually received.

The disclosure must be in writing and must be made in a manner that is reasonably likely to come to the attention of the donor. For example, a disclosure in small print within a larger document might not meet this requirement.

In the following three circumstances, the disclosure statement is not required.

(1) Where the only goods or services given to a donor meet the standards for "insubstantial value" set out in section 3.01, paragraph 2 of Rev. Proc. 90-12, 1990-1 C.B. 471, as amplified by section 2.01 of Rev. Proc. 92-49, 1992-1 C.B. 987 (or any updates or revisions thereof);

(2) Where there is no donative element involved in a particular transaction with a charity, such as in a typical museum gift shop sale.

(3) Where there is only an intangible religious benefit provided to the donor. The intangible religious benefit must be provided to the donor by an organization organized exclusively for religious purposes, and must be of a type that generally is not sold in a commercial transaction outside the donative context. An example of an intangible religious benefit would be admission to a religious ceremony. The exception also generally applies to de minimis tangible benefits, such as wine, provided in connection with a religious ceremony. The intangible religious benefit exception, however, does not apply to such items as payments for tuition for education leading to a recognized degree, or for travel services, or consumer goods.

A penalty is imposed on charities that do not meet the disclosure requirements. For failure to make the required disclosure in connection with a quid pro quo contribution of more than $75, there is a penalty of $10 per contribution, not to exceed

$5,000 per fundraising event or mailing. The charity may avoid the penalty if it can show that the failure was due to reasonable cause.

Please note that the prevailing basic rule allowing donor deductions only to the extent that the payment exceeds the fair market value of the goods or services received in return still applies generally to all quid pro quo contributions. The $75 threshold pertains only to the obligation to disclose and the imposition of the $10 per contribution penalty, not the rule on deductibility of the payment.