

G I F T S O F
N O N T R A D I T I O N A L
A S S E T S

a donor's guide

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A GUIDE TO MANAGING Capital Gains

Tweak your imagination. Assume you know about the usual and ordinary kinds of charitable gifts: cash, listed securities or real estate. Then suppose you possess a different kind of asset you might donate to us—but it doesn't seem to fit the typical mold. Maybe no one ever suggested to you that this sort of gift would be acceptable.

Now take a moment to think “outside the box” of traditional contributions. There are perfectly sound ways—familiar both to us and the IRS—to reach your philanthropic goals by other advantageous means. These include gifts of option stock, closely held stock, tangible personal property, intangible assets, life insurance and retirement plan benefits.

The Benefits of Philanthropy

Why do this? Primarily, because you feel strongly about supporting our vital needs, and you want to share your good fortune. In addition, you can achieve substantial income tax savings by making a charitable gift.

The actual income tax you save by the charitable deduction depends on your marginal income tax rate and any state or local tax deductions. For example, if you're in the highest federal bracket with applicable state and local income taxes, the actual cost of your charitable donation may be little more than half of its value to us. For property held long term to be deductible at fair market value with no tax on appreciation, the ceiling on

your current-year deduction generally is 30 percent of adjusted gross income, with a five-year carryover for any excess.

Sometimes the tax rules vary somewhat for a nontraditional asset, so it pays to know how to maximize your tax benefits. We'll tell you about some assets that fall into the out-of-the-ordinary category—quite possibly something you own. And we'll tip you off to special tax rules of which you need to be aware.

Option Stock

An incentive stock option is a form of compensation where your corporate employer grants you the right to purchase the company's stock at some time in the future at a specified price. Generally you don't realize taxable compensation at the time the option is granted or exercised, provided you don't dispose of the stock until the later of two years from the date the option was granted or one year from the date you received the shares upon exercise.

Assuming you wait to dispose of the stock after the holding period, you won't receive taxable compensation but there may be taxable capital gains. These are equal to the difference between the amount you receive in the disposition and the amount you paid when exercising the option. You must hold the stock at least 12 months after exercise to obtain long-term capital gains treatment.

Donating option stock: As long as you hold the stock for the required holding period—at least two years from the grant of the option and one year after its exercise—your outright

charitable gift of the acquired stock qualifies for the same deductibility as any gift of appreciated long-term capital gain property: a charitable deduction at fair market value, subject to the 30 percent ceiling, and no capital gain imputed to you.

Closely Held Stock

The stock you own in a closely held corporation can be utilized to make a gift to us. If you're the sole owner of stock in a profitable corporation, this is a good way to be philanthropic at relatively low personal cost. This can also be useful if you're a major stockholder in such a company and want to reduce your ownership without incurring capital gains taxes.

If the S corporation makes a contribution directly to a charitable organization, that contribution deduction will flow through to you as the shareholder. Thanks to a fairly recent tax law change, you can even contribute shares of S corporation stock to us without terminating the corporation's S election.

As such donations are illiquid and we may need cash for current needs, we may elect to turn the gift into cash by selling the stock. Generally the logical buyer is the closely held corporation. While this may be desirable from your standpoint, you should be careful to ensure that your gift is made without strings. If the IRS suspects there is any implied understanding or agreement that requires this action, it may seek to attribute any gain on the sale to you. Normally, however, we prefer not to be invested in nonmarketable securities, and most closely held corporations generally prefer not to have new outside shareholders.

A gift of stock followed by redemption is a good way to use cash in your closely held corporation for your charitable goals without having to pay yourself a taxable dividend first.

Donating closely held stock: The IRS no longer challenges properly executed transactions of this kind, but expert assistance is advisable. There may be a further advantage if your company has profits that need to be distributed in one manner or another to avoid a penalty tax on accumulated earnings. In order to deduct more than \$10,000, you'll need to obtain an independent qualified appraisal meeting specific IRS requirements and file a summary with your tax return.

Tangible Personal Property

Perhaps you own certain works of art, antiques or other collectibles (not created by you) that you might be willing to contribute. These items are fully deductible at their fair market value, with no tax on the appreciation, provided the organization uses the items in ways related to its normal exempt purposes. For example, the gift of a painting to an art museum would be fully deductible up to 30 percent of your adjusted gross income with five-year carryover for any excess. The gifts of such assets not for a related use are deductible only at your cost basis or their current fair market value, whichever is less, but up to 50 percent of adjusted gross income. If the tangible personal property is created by you, the charitable deduction is limited to cost basis.

Donating tangible personal property: Consult the charitable organization in advance of making a gift of tangible personal property to be sure it's acceptable and related to the organization's exempt purposes. In order to deduct more than \$5,000 per item or group of similar items, an independent appraisal is required. Easier (though still detailed) reporting rules apply for gifts valued at \$5,000 or less.

Intangible Assets

Stocks and bonds are typical forms of intangible personal property for charitable contributions. But individuals sometimes possess other types of intangible assets, such as copyrights, patents, and oil and gas interests. If you own any of these intangibles, think about the feasibility of donating the asset.

Copyrights: Under a rule that limits an income tax deduction for a gift of ordinary income property, an author or an artist can't deduct more than the cost basis of a manuscript, work of art or the related copyright. If you own both the artwork and the copyright, you must contribute both to receive a deduction. If you inherited a work from the artist, however, the ordinary income property restrictions disappear, and you can deduct the full fair market value of the donated work—the artwork, however, must be put to a “related use” as defined earlier.

Patents: A patent may make an ideal contribution because, unlike a work of art or a copyright held by the artist or author, a patent is treated as a capital asset even in the hands of the inventor. Assuming you contribute your entire interest in the patent, any resulting gain is treated as long term. So you may

contribute it and receive a deduction equal to its fair market value (normally based on the expected royalty payments).

Oil and gas interests: These come in many forms, such as fee, leasehold, operating or royalty interests, and they may be owned directly or indirectly. As a result, their contribution involves special considerations. For example, if the oil and gas interest is deemed to be a capital asset in your hands, in certain circumstances it's treated as a deductible gift of property rather than an anticipatory assignment of income. But where it's a production payment, you're not entitled to an immediate deduction when you make the gift. Instead, you include the payments as income when the charitable organization receives them, and you would presumably receive an offsetting charitable deduction.

If you own more than one interest in the oil and gas interest, you must contribute all of your interests to receive a charitable deduction. A gift of only some of your interests does not qualify.

Donating atypical intangible assets: The intangibles just described can be suitable charitable contributions in the right circumstances. A professional opinion is advisable to make certain that you can realize the desired tax savings and the charitable organization can benefit from your gift.

Life Insurance

A policy on your life is a hidden asset that could make an ideal charitable gift. Originally you may have intended the policy's death benefits for a purpose that's no longer relevant, such as a beneficiary now deceased, education of children now grown or a

mortgage now paid off. When these purposes are no longer valid, a policy with cash surrender value can serve a greater purpose when given to us, enabling us to use the cash for our pressing requirements.

The donation of a policy on which premiums remain to be paid is deductible at slightly above its cash surrender value. The tax deduction for a gift of a paid-up policy is generally its replacement cost. (In either case, your deduction can't exceed your investment in the policy.) The charitable organization must have an insurable interest in the donor's life under state law, but this is true of most states.

Donating a life insurance policy: Ask our representative to affirm our insurable interest and explain how you can determine your income tax deduction on any policy you might donate.

Retirement Plan Benefits

Like many Americans, you may find that your qualified retirement plans are a major resource—possibly even comprising most of your overall assets. For both practical and tax reasons, a charitable contribution of plan assets may make more sense in your case than a conventional gift of cash, securities or other property.

The term “qualified retirement plan” includes pension plans, other profit-sharing and stock bonus plans including 401(k) plans, employee stock-ownership plans (“ESOPs”), plans for self-employed persons (“Keogh” plans) and section 403(b) tax-sheltered annuities for employees of tax-exempt organizations.

The traditional Individual Retirement Account (“IRA”) is a similar tax shelter.

If you’re past age 70½, you have no choice but to begin receiving minimum distributions from a qualified plan. Perhaps you don’t need these payments for your current or long-term financial security. You could donate these distributions to us, thereby reducing or eliminating entirely the income tax that you would otherwise pay.

If you’re over age 55, you may begin to receive “substantially equal periodic payments” over your life expectancy from an IRA and subsequently, after at least five years of such payments, terminate them without imposition of the 10 percent penalty tax. A series of distributions could be structured for the specific purpose of funding a current charitable gift, providing that you won’t need the funds in question for the support of yourself or your family.

After your lifetime, the gift of an IRA or other retirement account can be the most tax-effective way to benefit us, resulting in the least impact on the shares of your individual heirs. That’s because such accounts are often exposed to both income taxes and estate taxes at a combined marginal rate of as much as 49 percent.

Donating retirement plan benefits: A gift during your lifetime from a qualified plan or IRA may be made only by withdrawing funds from that account. As a general rule, you’re subject to income tax on these withdrawals, but an offsetting charitable deduction is available for the amount of the

distribution you give to us (subject to the 50 percent of adjusted gross income limitation). To make a gift at death, name us on the plan's beneficiary designation form. If you're married, your spouse will need to sign a form waiving rights to the plan proceeds.

Explore Valuable Benefits of the Atypical Gift

For years you've heard all about donating cash and listed securities. Now you know there are exceptional advantages to contributing all sorts of "nontraditional" assets. We welcome the opportunity of helping you and your professional advisors determine the most cost-effective means of achieving your personal and philanthropic goals.

The information in this publication is not intended as legal advice. For legal advice, please consult an attorney. Figures cited in examples are based on current rates at the time of printing and are subject to change. References to estate and income tax include federal taxes only; individual state taxes may further impact results.

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