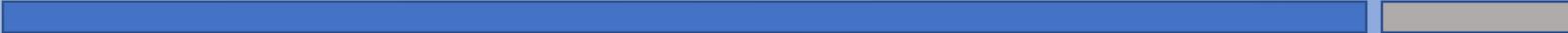


Mid-Atlantic Fellows Institute



Charitable Entities & Charitable Giving: An Overview

November 8, 2019

Edward Jay Beckwith, Partner
BakerHostetler LLP
Washington, D.C.
ebeckwith@bakerlaw.com

2019 Copyright Edward J. Beckwith.

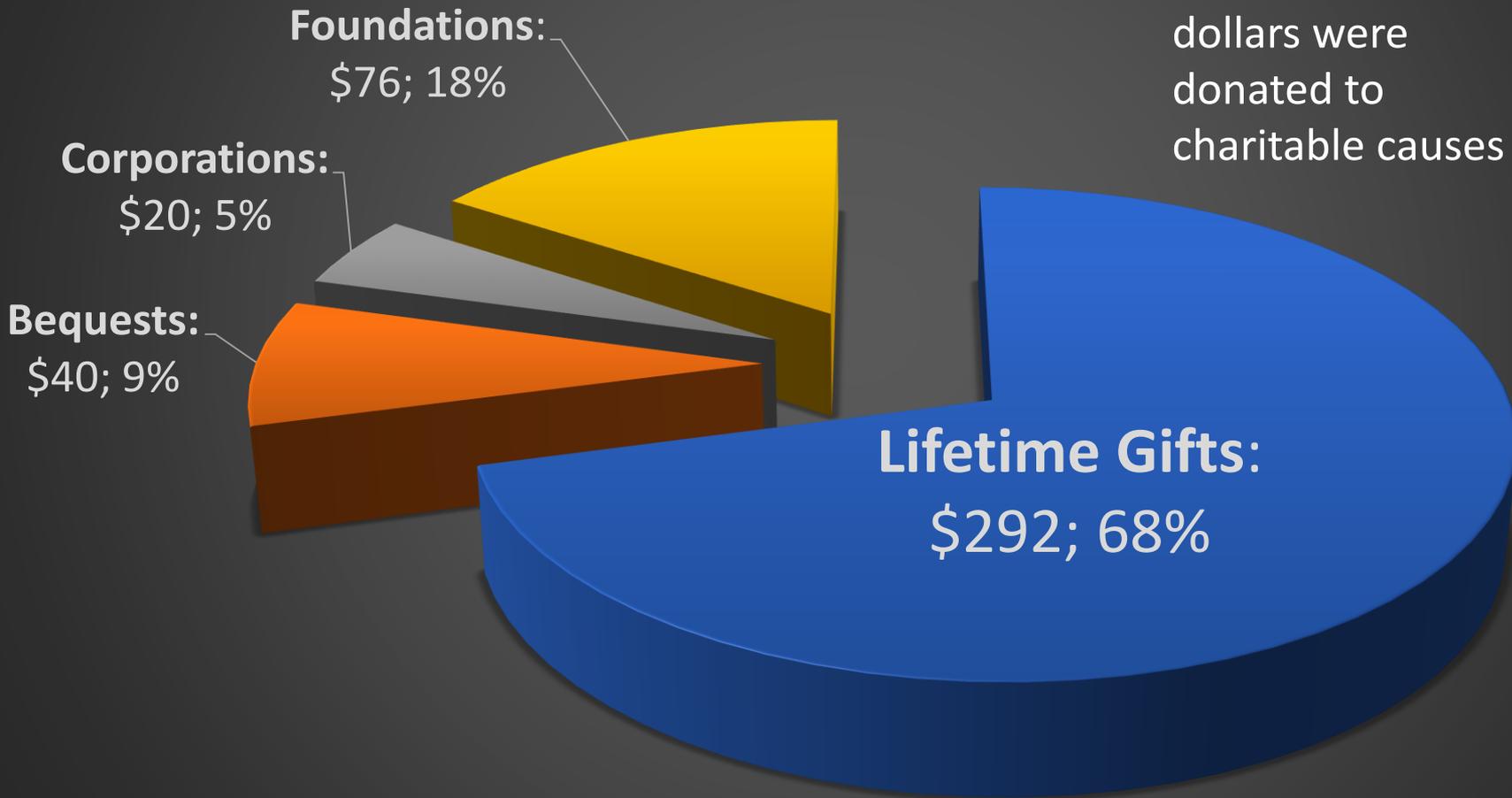


Philanthropy

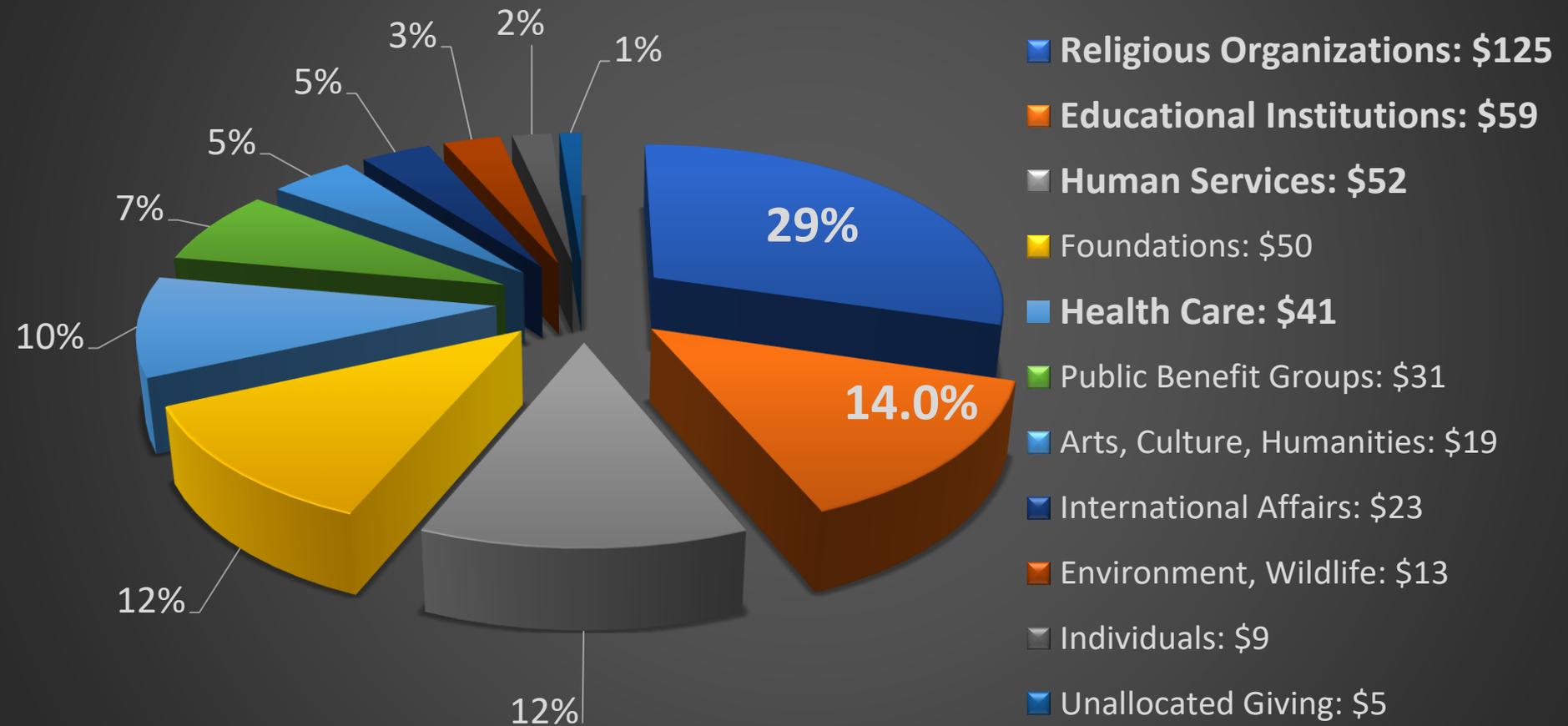
- Etymology: The love of humanity
- Merriam-Webster: Goodwill to fellow members of the human race and promotion of human welfare by an act or gift done or made for humanitarian purposes or an organization distributing or supported by funds set aside for humanitarian purposes

Scope of Philanthropy

In 2018, 428 billion dollars were donated to charitable causes



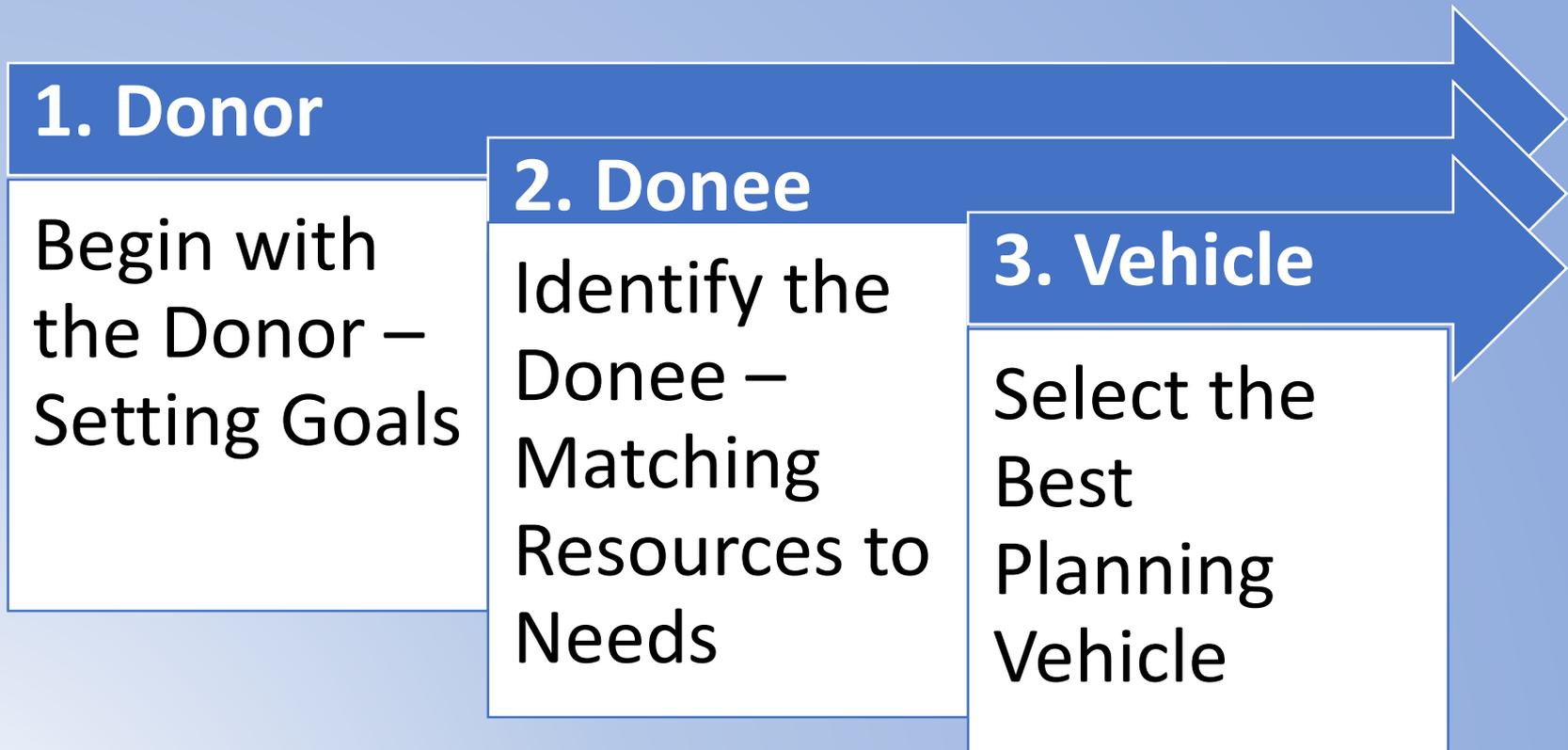
Where the Contributions Go



Philanthropic Personalities and Motivations

Communitarian	Doing good makes sense
Investor	Doing good is good business
Socialite	Doing good is fun
Altruist	Doing good feels right
Devout	Doing good is God's Will
Repayer	Doing good in return
Dynast	Doing good is a family tradition

Donor Centric Analysis

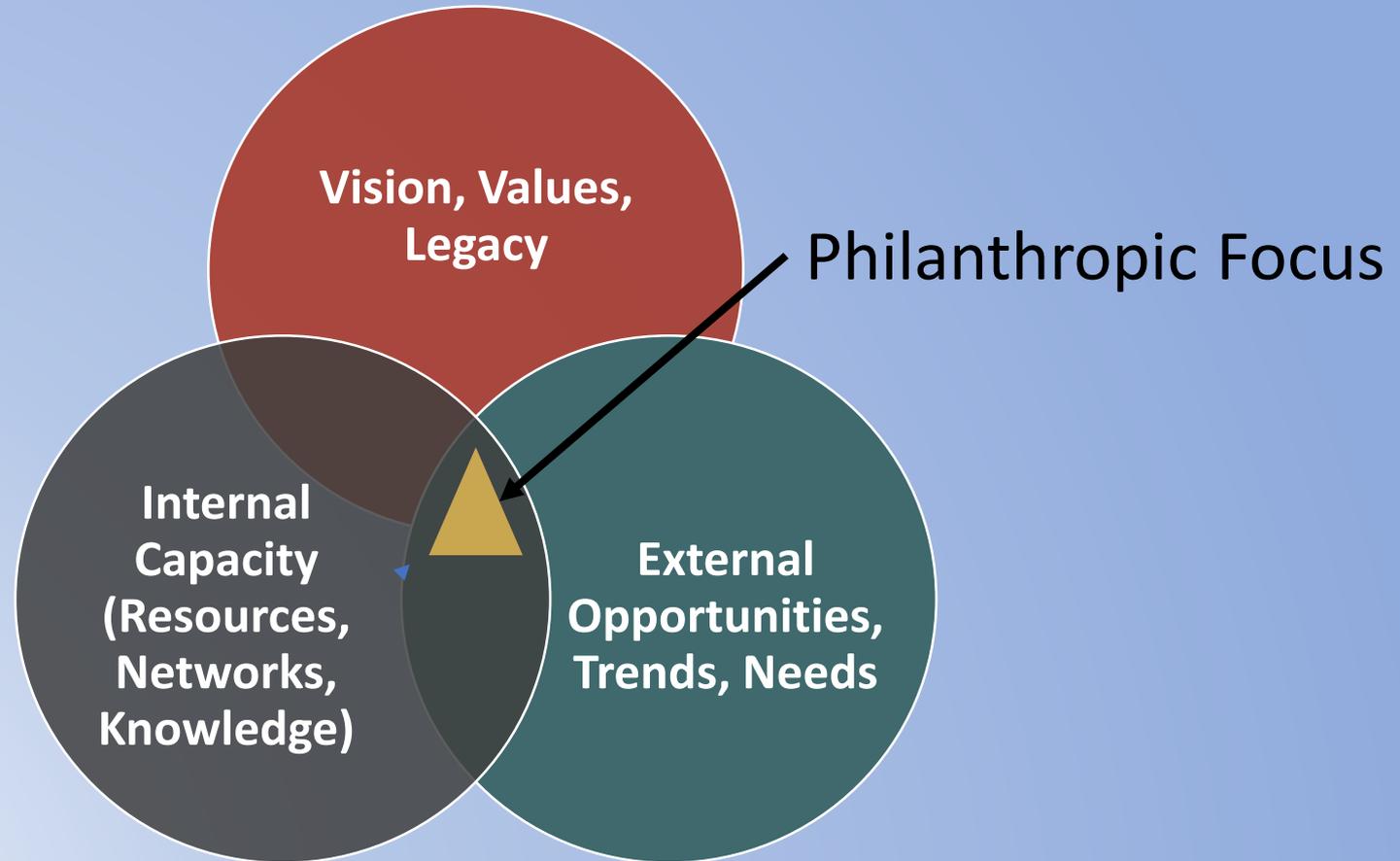


If you could change one thing in the world, what would it be?

The Philanthropic Discussion

- A charitable gift is not a product – it is part of a comprehensive process and a partnership
- The planning team – charitable donees working with the donor’s advisors
- Developing a vision: incorporate the philanthropic personality into mission, vision, and values
- Matching the resources with needs
- Evaluating potential charitable donees

Finding Philanthropic Focus



Philanthropists and Advisor Conversation Topics

Resources	<ul style="list-style-type: none">• Present and future commitments• Tax considerations: present and future• Dollar amounts and other assets• Time• Staffing
Goals	<ul style="list-style-type: none">• Goals dictate resource type, amount, and timing• Specific topic, geographic, or persistent problem to address• Immediate results versus long-term• Risk profile• Define success
Family Involvement	<ul style="list-style-type: none">• Gauge level of interest• Seek input and perspective: shaping the philanthropic vision versus coming onboard



Planning Basics

What do I want to give?

- Ordinary Income Property
- Capital Gain Property
- Income in Respect of a Decedent

To what?

- Public Charity
- Private Foundation

How is the gift to be arranged?

- Outright or in Trust
- Partial Interest
- Benefits to Donor
- Fulfilling a Pledge

Family Goals and Strategies

- Objectives of the Family
 - Return – value to be extracted from the business
 - Taxes – efficiency of the strategy on an ‘after-tax’ basis
 - Liquidity – amount and timing
 - Diversification – ability of the strategy to reduce overall portfolio risk
 - Control – maintain, surrender or share
- Strategy Considerations to Achieve Charitable Goals of the Family
 - Maximize the tax benefits of a charitable contribution
 - Select the appropriate asset (including the business itself) to be contributed
 - Structure the gift to supplement cash flow available to the family
 - Involve family members in management or deployment of the charitable gift
 - Coordinate with the family’s succession plan for the business
 - Generational succession and control of vehicle

Practical Gift Planning Funding Mechanisms

- Outright
 - Cash Gifts
 - Gifts of Closely-Held Stock
 - Bargain Sales
- Partial Interests
 - Trusts
 - Deductible Non-trust Split Interests
 - Remainder Interest in a Personal Residence or Farm
 - Undivided Portion of Taxpayer's Entire Interest
 - Qualified Conservation Contributions

Practical Gift Planning Funding Mechanisms

- Life Income Vehicles and Split Interest Gift Recipients
 - Charitable Remainder Annuity Trust
 - Charitable Remainder Unitrust
 - Charitable Remainder in a Qualified Terminable Interest Property Trust
 - Pooled Income Funds
 - Charitable Gift Annuity
- Charitable Lead (Annuity and Uni-) Trusts

Types of Charitable Gifts

- Outright Cash or In-Kind Gifts (e.g., Securities, Closely-Held Stock or retirement plans, real estate, artwork, cars)
- Certain Gifts in Trust (§170(f)(2))
 - Life Income Vehicles: Charitable Remainder Trusts; Charitable Gift Annuities and Pooled Income Funds
 - Charitable Lead Trusts
 - Wholly charitable trusts
- Bargain Sales (§170(c); 1011(b))
- Certain Partial Interest Gifts (§170(f)(3)(B))
 - Remainder Interest in a Personal Residence or Farm
 - Undivided Portion of Taxpayer's Entire Interest
 - Qualified Conservation Easement Contributions (§170 (h))

Tax Considerations

- No charitable deduction unless taxpayer itemizes
- Percentage Limitations: applied to the donor’s “contribution base” (AGI without NOL carryback)

Type of §501(c)(3)	Cash/Ordinary income/Short-Term Capital Gain	Long-Term Capital Gain
Public Charity, Private Operating Foundation (POF) or pass-through Private Foundation	Outright: 50%/60% (§170(b)(1)(A)) In Trust: 30% (§170(b)(1)(B))	Outright: 30% (§170(b)(1)(B)) In trust: 20% (§170(b)(1)(C))
Private Foundation (PF)	Outright or in Trust: 30% (§170(b)(1)(B))	Outright or in Trust: 20% (§170(b)(1)(D)) Deductible value limited to basis unless gift is qualified appreciated stock

Tax Considerations (Cont.)

- Five-Year Carry Forward §170(d)
- Section 68 limitation on itemized deductions may also reduce deduction (Note that this limitation has been suspended for taxable years 2018-2025)
- Corporate Gift Limit: 10% of pretax net income (computed without taking into account any NOL or capital loss carrybacks) (170(b)(2))

See IRS Pub 526, *Charitable Contributions*

Substantiation Requirements

- Receipt Requirement:
 - Subject to de minimis safe harbors, “contemporaneous acknowledgment” needed, including whether goods/services were provided, describing goods/services and good faith estimate of value of the non-deductible goods/services provided IF:
 - Donation is \$250 or more OR
 - Donation is \$75 or more and the donor received something in return (other than token benefits, certain membership benefits, or intangible religious benefits);
- Donation of \$500 or more:
 - Receipt must contain donee’s name, date and location of the contribution, and a description of the property
 - If noncash, donor must file Form 8283, Noncash Charitable Contribution with income tax return
 - Treas. Reg. § 1.170A-13(b).

Substantiation Requirements (Cont.)

- Donations over \$5,000 (other than cash or publicly-traded securities) and over \$10,000 in closely-held stock: obtain qualified appraisal and attach summary to return.
- Donated artwork with an aggregate value of \$20,000 or more: photograph and a copy of signed appraisal required.
- Donations over \$500,000: attach qualified appraisal to return.

Contributions Subject to Special Substantiation Rules or Deduction Limitations

- Gifts of clothing and household items
- Fractional or Future Interests in Tangible Personal Property
- Taxidermy
- Inventory, scientific property, computer technology and equipment
- Automobiles, boats, planes
- Gifts of property subject to debt
- Patents and other intellectual property

Considerations in Selecting a Charitable Donee

- Donor's relationship to the nonprofit
- Availability of investment management
- Amount, nature, restrictions, and retained control of potential assets
- Ability for Donee to raise funds from third parties
- Desire for anonymity and privacy
- Tax on investment income
- Minimum distribution requirements
- Use of specific planned giving vehicles which could defer funding until death
- Burden of administration, tax filings, and management costs
- Grants
 - Nature and location of anticipated grantees
 - Ability to make scholarship grants to individuals
 - Donor input for grant-making

Component Funds at a Public Charity

- Unrestricted funds
- Designated funds
- Field of interest funds
- Donor advised funds

Restrictions on Funds

- Source can be the donor, donee, solicitation materials, board resolution, or operation of law
- Fashioning restrictions
 - How rigid can the donor be?
 - How rigid should the donor be?
 - Can the restrictions be modified or deferred?
- Who can enforce restrictions?
 - Donor
 - Person benefited by gift
 - State Attorney General
- Court modification
 - Doctrine of Cy Pres prevents the failure of charitable purpose
 - Doctrine of Deviation removes administrative obstacles impeding accomplishing the charitable purpose

Types of 501(c)(3) Organizations

Types of 501(c)(3) Organizations

- Essentially Four Basic Types of Section 501(c)(3) organizations:
 - Private Foundations
 - Organization engaging in inherently public activity
 - Publicly supported organizations
 - Supporting organizations

Types of 501(c)(3) Organizations

- Public Charities (PCs): Those organizations described in §509(a)(1-4)
 - Basic idea is broad public support and broad oversight
- Private Foundations (PFs): all other §501(c)(3) organizations
 - Often created by a few people, a business, or a family

Types of Public Charities (PC)

- Per Se Public Charities (§§ 509(a)(1); 170(b)(1)(A)(i-v))
- Publicly Supported Organizations (§§ 509(a)(1) and 170(b)(1)(A)(vi))
- Gross Receipts Organizations (§509(a)(2))
- Supporting Organizations (SOs) (§§ 509(a)(3) and 170(b)(1)(A)(viii))

Requirements for 501(c)(3) Exemption

- “Corporations, and any community chest, fund, or foundation...”
- “Organized and operated exclusively” (interpreted as primarily) for exempt purposes
- No private inurement
- No campaigning and no substantial lobbying

Per Se Public Charities

Under §§ 509(a)(1) and 170(b)(1)(A)(i-v)

- Organizations automatically qualified as public charities, including:
 - Churches
 - Schools, colleges and universities
 - Hospitals and medical research organizations
 - Governmental Units
 - Certain agricultural research organizations

Publicly Supported Organizations Under 509(a)(1) & 170(b)(1)(A)(vi)

- 1/3 Support Test (Treas. Reg. § 1.170A-9(f)(2)):
 - “Normally” at least 1/3 of total support from governmental units or the general public
- OR
- Facts and Circumstances Test (Treas. Reg. § 1.170A-9(f)(3)):
 - “Normally” at least 10% public support, and other public features (e.g., continuous and bona fide fundraising program, community board, facilities/services/programs available to public, varied sources of support)
- Numerator Limitation: Cap of 2% per donor

Gross Receipts Organizations Under §509(a)(2)

- More than 1/3 of total support from donations from public/government OR receipts from conducting exempt activities (admissions, sales, performing services, providing facilities)

AND

- No more than 1/3 of total support from investment income and Unrelated Business Income
- Numerator Limitations:
 - Cap of \$5,000/1% per donor
 - Donations from disqualified persons excluded

Supporting Organizations (SO) Generally Under §§ 509(a)(3) and 170(b)(1)(A)(viii)

- Excluded from definition of PF based on close relationship to PCs
- 3 types of SOs:
 - Type I (parent-sub): “Operated, supervised, or controlled by” one or more publicly supported organizations;
 - Type II (brother-sister): “Supervised or controlled in connection with” one or more such organizations, or
 - Type III: “Operated in connection with” one or more such organizations

Supporting Organization (SO) Tests

- All SOs required to meet 3 tests:
 - Organizational Test: must be organized and operated exclusively for the benefit of one or more PCs
 - Operational Test: must be operated, supervised, or controlled by or in connection with one or more PCS
 - Control Test: must not be controlled directly or indirectly by one or more disqualified persons (other than a foundation manager)
- Additional Rules for Type IIIs:
 - notification requirement
 - must meet responsiveness and integral part tests

Private Foundations Generally

- Funded by a few donors and closely controlled
- Types include:
 - Private Operating Foundation (POF) (§170(b)(1)(A)(vii) and (F)(1)): uses assets to conduct its own charitable programs/activities rather than making grants to other organizations
 - Pass-Through Foundation (§170(b)(1)(A)(vii) and (F)(2)): distributes all receipts annually;
 - Private Grant-Making Foundation; and
 - Corporate Grant-Making Foundation

Private Foundation Excise Taxes

- Net investment income tax of 1-2% (§4940)
- Self-dealing (§4941)
- Minimum Annual Distributions (generally 5% of assets) (§4942)
- Excess Business Holdings (§4943)
- Jeopardizing Investments (§4944)
- Taxable Expenditures (§4945)
- Private operating foundations exempt from undistributed income tax (§4942(j)(3))
- “Exempt operating foundations” exempt from net investment income tax (§4940(d))

Public Charities vs Private Foundations

Features	Public Charities	Private Foundations
Deduction Percentage Limitations under §170(b)(1)	“50% charities”	“30% charities”
Sanctions/Excise taxes	Excess lobbying (§4911), excess benefit transactions (§4958) and prohibited tax shelter transactions (§4965)	Private foundation rules (§§4940–4945) and prohibited tax shelter transactions (§4965)
Annual Reporting to IRS (§6033(c))	Form 990/990EZ/990-N e-postcard	Form 990PF; no EZ or postcard option
Grant oversight	No expenditure responsibility required	Expenditure responsibility for certain grants (§4945)
Lobbying	Insubstantial lobbying expenditures ok (§501(h))	No lobbying
Termination Tax (§507(a))	No	Yes in certain circumstances



Choice of Entity

What Form Should the Entity Take?

- Nonprofit Corporation
- Trust
- Limited Liability Company (LLC)
- Unincorporated Nonprofit Association

Key Entity Comparisons*

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Formalities/ Ease of formation	Formal filing with State agency (e.g., articles of incorporation); notice of formation to State A.G. (state dependent)	Trust agreement; notice of formation to State A.G. (state dependent)	Formal filing with State agency (e.g., articles of organization)	No formalities and minimal legal structure (bylaws or constitution)
Flexibility/ Ease of modification	Very flexible; easily modified (member/board resolution & State filing)	Least flexible; more difficult to modify (court proceeding usually needed)	Very flexible; easily modified (member resolution & State filing)	Very flexible; easily modified (member/board resolution)

*Characteristics will vary State to State; consult local State law

Key Entity Comparisons (Cont.)

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Legal Certainty	High degree of legal certainty; statutory default rules & well developed case law	Less certain if no trust code; more certain if trust code in place	Statutory defaults in most states but less certain as tax-exempt organizations	Least certain with few, if any, statutory default rules; may not be respected as separate entity
Taxable or Tax-exempt	Either	Either	Either, unless enabling statute requires business purpose	Either

Key Entity Comparisons (Cont.)

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Personal liability for debts or liabilities of entity	No (RMNPCA §8.30(d))	Yes under Restatement (Second) Trusts (§261); No under UTC (§1010)	No (ULLCA §304)	Yes, except as modified by statute (e.g, No under UUNAA (§8))
Personal Liability for Breach of Duty	Gross negligence, not errors of judgment; (RMNPCA §8.30(d))	Mere negligence per Restatement (Second) Trusts, including for acts of agents (§264); lower standard under UTC §804	Gross negligence or reckless conduct, willful or intentional misconduct, or knowing violation of law (ULLCA §409)	Mere negligence, except as modified by statute (e.g., UUNAA §§17, 22)

Key Entity Comparisons (Cont.)

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Standard of Care	(1) good faith, (2) with care of an “ordinarily prudent person in a like position would exercise under similar circumstances” and, (3) in manner reasonably believe is in best interest of entity (RMNPCA §§8.30; 8.42)	Varies but either as a prudent person (1) dealing with own property (under Restatement 2 nd Trusts, §174) OR (2) “considering the purposes, terms, distributional requirements, and other circumstances of the trust” (UTC § 804)	Modified business judgment rule (see above- must refrain from gross negligence, etc.) with good faith and fair dealing (ULLCA 2006 §409(c));	Member: no duty; Manager: (1) good faith, (2) in a manner reasonably believe is in the best interest of the association, (3) with care a prudent person in a similar position/similar circumstances, (4) after reasonable inquiry (UUNAA §§17,22)



Key Entity Comparisons (Cont.)

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Indemnification/Exculpation	Mandatory and permissive indemnification in Model Act if no improper financial benefit or unlawful distributions, no intentional infliction of harm or intentional criminal act (RMNPCA §8.51, 8.52)	No exculpation for “bad faith” or reckless indifference re: trust purposes or beneficiary interests (acts beyond ordinary negligence); may be invalid if drafted by trustee (UTC §1008)	More limited than NP Corporation but available by statute and/or in governing documents (ULLCA §408)	More limited than NP Corporation but available if person complies with statutory duties (RUUNAA §26)

Key Entity Comparisons (Cont.)

Features	NP Corporation	Trust	LLC	Unincorporated NP Association
Volunteer Protection	Person acting without compensation protected from all but gross negligence (full standard in trust box) under Federal Volunteer Protection Act and more protection in some states	Same (protection excludes willful or criminal misconduct, gross negligence, reckless misconduct, and conscious, flagrant indifference to rights or safety of person injured)	same	same

Questions, Thoughts & Comments



Contact the Presenter

Edward Jay Beckwith, Partner

BakerHostetler LLP

Washington, D.C.

(202) 861-1646

ebeckwith@bakerlaw.com

www.bakerlaw.com

