TRANSPARENCY COUNTS:
How Understanding Reporting Obligations Can Satisfy Donors and the IRS

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Charitable organizations occupy a hallowed position in the United States—a position hallmarked by exemption from federal income tax. Because of this privileged status and the charitable nature of their missions, charities are largely financed by donations. Part of the special relationship between charities and donors is derived from the tax-favored nature of their donations. Because both the donor and the charity receive tax benefits with respect to charitable donations, the relationship is constrained on both sides by regulations affecting donors and regulations affecting the charity. In short, to preserve tax-favored status, both the charity and the donor must be entirely transparent with the IRS.

Tax Treatment of Donors—the Contemporary Written Acknowledgment

Donors are permitted to deduct some or all of their donations to charitable organizations, with certain limitations imposed by the Internal Revenue Code. Until 1993, donors were not required to substantiate the value of their charitable donations, leading to widespread abuse, both real and perceived. To curb overvaluation of charitable donations and other abusive tactics, Congress enacted Code Section 170(f)(8), which requires donors to substantiate charitable donations using bank statements, canceled checks, or, in the case of donations greater than $250, a contemporaneous written acknowledgment from the charity.

The contents of the contemporaneous written acknowledgment will differ depending on the size of donation, but must include at least the donor's name, the charity's name, the cash amount of the donation or a description of the donation (if other than cash), the date of the donation, and the amount and type of goods or services provided by the charity to the donor, if any (a so-called "quid pro quo contribution"). Donations greater than $500, particularly donations of cars or boats, require a higher level of disclosure, including the charity's intended use of the donation. These are typically documented using IRS Form 1098-C. Further, to deduct a donation over $500 on the donor's tax return, the donor must attach IRS Form 8283, which must be signed by an authorized representative of the charity.

Importantly, the charity's written acknowledgment should not recite a value for noncash donations, since the burden of substantiating the value of such donations is on the donor. In fact, any noncash donation greater than $5,000 must be substantiated by a written appraisal; however, establishing the value of donations is beyond the scope of this article.

If the donor does not produce a contemporaneous written acknowledgment to substantiate a charitable deduction or if the organization's acknowledgment is deficient in any way, the donor's deduction can be denied. So to support and foster the symbiotic relationship with donors, each charity is well advised to issue accurate and timely written acknowledgments to its donors.

In this respect, "contemporaneous" doesn't necessarily require that each acknowledgment be issued at the time of the donation; rather, the charity must simply acknowledge donations before the

donor files a tax return in which the donor claims a charitable deduction.[1] To be "accurate," the charity must only make a good-faith estimate of the value of the goods and services given to the donor in a quid pro quo transaction, based on any reasonable method of valuation.

Charitable Organizations—Reporting Quid Pro Quo Contributions

In some instances, the charity is required to disclose the existence and value of goods or services rendered to a donor, regardless of the size of the donation received. Disclosure must occur anytime the charity gives goods or services having a value greater than $75 to any donor in consideration for the donor's contribution to the charity. The disclosure must inform the donor that the value of the donor's charitable gift is limited to the amount by which the value of the donation exceeds the value of the goods or services provided by the organization and must give a good-faith estimate of the value of the goods or services provided to the donor.

Accurately reporting the value of the goods or services provided to the donor is not always straightforward, although in many cases the value is simply the approximate cost of obtaining the same goods or services on the open market. For example, if a donor purchased tickets to a benefit concert for $250 per seat, but could buy tickets to see the same (or similar) artist in an unrelated venue for $100 per seat, the charity could likely report the value of each concert ticket as $100. In such a case, the donor's contribution would count as only $150.

Certain exceptions apply to the quid pro quo transaction reporting requirement, and can generally be divided into three separate exceptions for (1) insubstantial goods, (2) membership benefits, and (3) intangible religious benefits. Goods are generally "insubstantial" if given to a donor in the context of a fundraising campaign, and the value of the goods is truly insubstantial in relation to the donation. The lapel pins, mugs, and pens often given out at organization events are common examples of insubstantial goods. Memberships also do not need to be reported unless the annual membership cost exceeds $75 or the donor receives excessive membership benefits. Because of their intangible nature, religious benefits do not need to be quantified, but are often reported. If none of these exceptions apply, and the charity fails to provide the appropriate written disclosure, the charity is subject to a $10 penalty for each failure to disclose. The penalty is capped at $5,000 per fundraising event.[2]

Although these reporting requirements are not terribly onerous, the applicable penalties for failing to comply can become significant and pale in comparison to the cost of poor donor relations. Therefore, every organization soliciting charitable donations from the public should review its gift acceptance policies to ensure that they comport with the applicable IRS guidelines.

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[1] Some exceptions apply, for example, the acknowledgement must be given to the donor within 30 days of a subsequent sale of a donated vehicle.

[2] There are a variety of regulatory parameters and limitations on each of these exceptions—consult a tax professional for more information.

About the author:

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