

## Gifts to Charities

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### *Sec. 2503(e) Exclusion for Payments of Educational or Medical Expenses*

The topic of the Autumn 2002 issue of *AKO Estate Planning & Tax Advisor* was gifts to individuals. In that issue, we promised to explain in greater detail the rules under Sec. 2503(e) of the Internal Revenue Code ("IRC") for direct payments of tuition or medical expenses made for another person. There are no limits on the amounts of such payments, and the payments are not considered gifts for gift tax purposes. The beneficiary of a qualified tuition or medical transfer does not need to be related to the taxpayer and an annual exclusion gift can still be made to the beneficiary.

Payments must be made DIRECTLY to the educational institution or medical provider and not to the beneficiary. Payments for books, supplies, dormitory fees and board do not qualify, nor do contributions to qualified tuition programs under IRC Sec. 529. Tuition for a student of any age, from pre-school through post-graduate qualifies, including tuition for part-time students. Medical payments can cover any type of expense that is deductible for income tax purposes, including physicians, dentists, prescription drugs and medical insurance premiums.

Sec. 2503(e) offers many ways to extend family gifting. Grandparents can pay a grandchild's tuition by writing the check directly to the educational institution, and continue to give the grandchild an annual \$11,000 gift (or \$22,000 if the grandmother and grandfather gift split). If aging parents can no longer afford to pay all their own expenses, their adult children, or anyone else, can pay their elders' medical bills directly without any gift tax consequences.

### *Now That You Know the Rules for Gifts to Individuals, Here are Some of the Rules for Gifts to Charities*

As we approach the holiday season and many of us make our year-end gifts to charity, we thought this would be an opportune time to discuss some of the rules governing the timing, deductibility and substantiation requirements of some of the more common types of gifts to charities.

Gifts of money—either by check or by credit card—are deemed to have been made when the check is mailed or when the credit card issuer posts the charge, as the case may be. Therefore, even a check mailed on December 31, 2002 will be considered a charitable gift made in 2002. Compare this with the rule for a gift made to an individual, which would require that the check be received and negotiated by the recipient in 2002 if it were to be considered a gift made in 2002. If the contribution is made to a charity having "public charity" or "private operating foundation" status (terms used by the IRC), the gifts of money to the charity are deductible up to 50 percent of the donor's adjusted gross income. If the gift is made to a "private foundation"



## who's who

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(another IRC term), the deductibility can be no more than 30 percent of the donor's adjusted gross income. If the amount of the gift exceeds the maximum allowable percentage of the donor's adjusted gross income, the excess can be carried forward for five years.

Gifts of long-term securities, that is, securities held one year or more, are, absent a special election which can increase the deductibility ceiling, deductible only up to 30 percent of adjusted gross income if made to a public charity or private operating foundation. Different rules apply if made to a private foundation. The deduction is based on the full present fair market value; the appreciation escapes tax. For securities trading on a stock exchange or over-the-counter market, or for closed-end investment company shares, fair market value is the mean between the high and low on the date of delivery (or bid and asked prices on the date of delivery if quoted high and low prices are not available). For open-end investment companies (such as most mutual fund shares), the fair market value is the closing public redemption ("bid") price.

Gifts of short-term securities are deductible up to 50 percent of the donor's adjusted taxable income if made to a public charity or private operating foundation. Lower percentages apply if made to a private foundation. In valuing a gift of short-term securities, however, the value of the gift is limited to the cost basis or present fair market value, whichever is less.

If a properly endorsed, physical certificate is mailed to the charity or to the charity's agent, the contribution is considered to be made on the date of mailing. If it is delivered to the charity by other means or if delivered by hand, the delivery date is the date the charity or the charity's agent actually receives it. If the donor delivers the certificate to the donor's bank or broker (or instructs his or her broker to transfer a security already in the donor's brokerage account) for transfer to the charity, the gift is completed on the date the stock is transferred into the name of the charity.

In order to deduct any gift of \$250 or more, the donor is required to obtain a contemporaneous written acknowledgment from the charity. The acknowledgment must be obtained by the donor by the *earlier* of the actual filing of his or her tax return for the year in which the gift is made or the due date (including extensions) for filing the donor's tax return for that year. Early filers, beware! ■

**Helpful Tips:** Donors wishing to contribute securities having fair market values less than their cost bases may be better off to sell the losing securities, use the losses to offset any gains, and make the charitable gifts with the cash proceeds of the sales.

Because different deductibility limits apply, depending upon whether the charity is classified by the Internal Revenue Service as a public charity, private operating foundation or private foundation, donors may wish to ask the charity for its classification before deciding how much, and what type, of property to give.

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