Douglas County Community Foundation
CELEBRATING 20 YEARS

Professional Advisor News

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"501(c) what?"
Sorting through jargon to determine deductibility

When tax season rolls around each spring, a new crop of questions may arise concerning clients' gifts to various organizations and whether those donations qualify as tax-deductible charitable contributions.

Keep in mind that Section 501(c) of the Internal Revenue Code lays out the requirements for organizations to be considered tax-exempt — a status for which an organization must seek IRS approval. Tax exemptions apply to certain types of nonprofit organizations; however, status as a nonprofit (which is a state law construct) does not necessarily mean that the organization will be exempt from federal income taxes.

Under Section 501(c), there are even different types of nonprofits that are recognized by the IRS as tax-exempt. To qualify under the Internal Revenue Code Section 170 charitable deduction for gifts to Section 501(c)(3) organizations, for example, the recipient must be organized and operated exclusively for "charitable, religious, educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and preventing cruelty to children or animals." "Charitable," according to the IRS, has a very narrow definition.

No doubt, many of your clients support not only 501(c)(3) charities, but also social welfare groups organized under Section 501(c)(4). Examples of social welfare groups include neighborhood associations, veterans organizations, volunteer fire departments, and other civic groups whose net earnings are used to promote the common good. Donations to social welfare groups are tax deductible in only certain cases (e.g., gifts to volunteer fire departments and veterans organizations). Chambers of commerce and other business leagues fall under Section 501(c)(6); donations to these entities are not tax deductible.

If you have questions about the tax deductibility of your clients' contributions to various organizations, please reach out to the team at DCCF. We are immersed in the world of Section 501(c) every single day and are happy to help you navigate the rules.

"If not 501(c), then what?"
Cautioning clients about crowdfunding

What if your clients make donations to entities that don't fall under a specific section of the Internal Revenue Code, but feel "charitable" nonetheless because the dollars are helping people in need? Perhaps a client has helped set up a dedicated account at a bank to provide scholarships to the children of an accident victim, or participated in a GoFundMe fundraiser to help a specific family. These, along with other crowdfunding platforms, typically do not meet the qualifications for a charitable organization under Section 501(c)(3), usually because the funds are earmarked for a particular person or persons.

According to a Lilly Family School of Philanthropy survey, nearly a third of respondents said they donate at least once a year to a crowdfunding venture, especially when responding to family members and close friends in need.

Even with the increase in popularity of crowdfunding and online fundraising platforms, the IRS has only just begun to issue guidance. Consider Private Letter Ruling 2016-0036. Here, the IRS referenced a notion it referred to as "detached generosity" and noted that giving to strangers on a platform such as GoFundMe did not generate the "quid pro quo" that is an automatic knockout punch for charitable deduction eligibility. Still, the IRS indicated that the absence of a quid pro quo is not enough to cause a transaction to rise to the level of a charitable contribution. Taxpayers and professionals still must pay close attention to the circumstances and facts of each situation.

Ice breakers:
Three easy openers to talk about philanthropy

Many advisors really want to bring up charitable giving in client meetings, especially while updates to tax and estate plans are underway. Indeed, many advisors believe they have a responsibility to raise the issue.

But how?

Addressing charitable giving priorities with clients does not need to be hard. The key is to be interested, relevant, and authentic. Here is a tip for each.

1. Show genuine interest.

Dale Carnegie's maxim, "To be interesting, be interested," is good advice for nearly every social or business encounter. Especially with charitable giving topics, showing interest is important because giving is very personal and emotional. When you are reviewing a client's tax return, for example, ask about the charitable organizations the client supports. You'll likely be amazed at the richness of the stories behind each gift.

2. Stay relevant.

Tax reform is on the minds of many clients. This gives you an opening to talk about potential changes to the tax rates and what might happen to capital gains treatment. Explore each client's balance of charitable interests versus leaving inheritances to family members. Charitable clients will be glad to know you are up to date on lobbying efforts of nonprofit sector leaders. Indeed, many charitable clients serve on nonprofit boards whose members also would find this information useful. For example, in its April 16, 2021 letter to Secretary of the Treasury Janet Yellen, the Charitable Giving Coalition noted that the charitable deduction is "unique" and "promotes a selfless act, incentivizing taxpayers to give more funds to charities than they would otherwise give."

3. Be authentic about COVID-19.

Nearly everyone has been affected by the pandemic in some way. Sharing your own experiences and impressions of 2020 and early 2021 will encourage clients to open up. Charitable giving is a natural topic of this conversation. According to a study conducted by Candid, U.S. foundations, corporations, and individual donors stepped up by granting more than $10.7 billion as of early 2021 to address pandemic-related challenges. "There is no doubt that philanthropy has responded to COVID-19 on a scale not seen before," note the study's authors. Inspiring statistics like these bring home the importance of charitable giving as part of a family's overall financial and estate plan. And of course, please reach out to DCCF for updates on how our board, staff, and donors are rallying to meet the COVID-19 challenges in our own community.

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