

Charitable Deductions and Contributions of Partial Interests in Property

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The transfer of a “partial interest” in property refers to one of two types of transfers: transfers of an undivided interest in the transferor’s entire interest in the property; and transfers of term, annuity, life estate, or remainder interests, so-called split interests, in property contributed in trust or not in trust.



INCOME AND TRANSFER TAX DEDUCTION FOR TRANSFERS NOT IN TRUST¹

General Rule

Internal Revenue Code (IRC) Section 170(f)(3)(A) provides the general rule that contributions of partial interests in property, not in a trust, are not deductible.² Note that there is no deduction allowed for contributing use of an item of property, which is considered a partial interest.³ Congress disallows a deduction for the use of property to prevent a double tax benefit to the donor: a lack of taxation on the income from the property used by the charity; and a charitable deduction for full rental value of the property.⁴ Likewise, an interest-free loan of money to a charity is not deductible because it is a partial interest in property.⁵ However, there are exceptions provided in IRC Section 170(f)(3)(B) for remainder interests in a residence or a farm, or an undivided portion of the donor’s entire interest in the property, or a conservation contribution.⁶

Undivided Fraction or All of the Donor’s Interest

An undivided portion of the donor’s entire interest in the item of property refers to a fraction or percentage of each and every substantial interest or right the donor owns in the property.⁷ Assume a donor owns a life estate in a building and donates a fraction of the life estate to a charity. The contribution of the fractional interest, not in trust, is deductible by the donor because it is a fraction of each substantial interest or right the donor has in the property.⁸ Likewise, if the donor contributed the entire life estate, not in trust, it would be deductible.⁹

If the owner of an annuity interest in a charitable remainder annuity trust,

presumably a unitrust, contributes that annuity interest to the remainder charitable beneficiary, not in trust, it is treated as a deductible contribution by the donor.¹⁰

If a donor gives a life estate to one charity and the remainder interest in the property to another charity, the contribution qualifies as a deduction of the donor's entire interest in the property at its fair market value.¹¹ However, if property is intentionally divided into separate interests to circumvent the partial interest rules, any such contribution is denied a deduction.¹²

Remainder Interest in a Residence or Farm

While a deduction is allowed for the contribution of a remainder interest in a residence or a farm, not in trust, a deduction is not allowed for the proceeds of the sale of the remainder interest if the remainder interest is required to be sold.¹³ The residence may be any residence of the donor and does not need to be the principal residence of the donor.¹⁴

A farm is defined as: any land used by the taxpayer or his tenant for the production of crops, fruits, or other agricultural products or for the sustenance of livestock. The term 'livestock' includes cattle, hogs, horses, mules, donkeys, sheep, goats, captive fur-bearing animals, chickens, turkeys, pigeons, and other poultry. A farm includes the improvements thereon.¹⁵

If property is subject to a mortgage, it is treated as a bargain sale. If the donor continues to make mortgage payments, they constitute additional contributions deductible to the extent attributable to the remainder interest.¹⁶ Depreciation must be taken into account on the contribution of a remainder interest in real property.¹⁷ The specific rules for depreciation are beyond the scope of this section.

Qualified Conservation Contribution

A qualified conservation contribution is defined in IRC Section 170(h) as a contribution:

- a) of a qualified real property interest;
- b) to a qualified organization;
- c) exclusively for conservation purposes.

A qualified real property interest is one of: 1) the entire interest of a donor other than a qualified mineral interest; 2) a remainder interest; and 3) a restriction (granted in perpetuity) on the use which may be made of the real property.¹⁸ A qualified organization is any of: 1) a governmental unit or a publicly supported charity described in clause (v) or (vi) of subsection (b)(1)(A) of IRC Section 170; 2) a publicly supported organization described in section 501(c)(3) which meets the requirements of section 509(a)(2); or 3) a support organization that meets the requirements of section 509(a)(3) and is controlled by a governmental unit or publicly supported charity,¹⁹ that uses the property for a conservation purpose as defined in IRC Section 170(h)(4).

Limitation on Charitable Contributions of Tangible Personal Property

For contributions made after August 17, 2006, IRC Section 170(o) limits the deduction for contributions of partial interests in tangible personal property, limiting the ability of donors to make fractional donations, or term interests, of art and other valuable tangible personal property to charities unless the charities ultimately own or have exclusive use of the entire property, as part of its exempt purpose, within the earlier of the death of the donor or ten years.

INCOME AND TRANSFER TAX DEDUCTIONS FOR PARTIAL INTERESTS CONTRIBUTED TO A TRUST²⁰

Qualified Annuity, Unitrust Interests, or Pooled Income Funds

No deduction is allowed for a partial interest, split interest, contribution to a trust, or typically a life estate, term, or remainder interest, unless the transfer is to a charitable remainder annuity trust or unitrust as described in IRC Section 664,²¹ a charitable income trust (charitable lead annuity or unitrust) pursuant to IRC Section 170(f)(2)(B), or a pooled income fund under IRC Section 642(c)(5).

The rules for deducting partial interests for income, estate, and gift tax purposes are quite complex and require additional research beyond simply reading this chapter.

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1. References to the Internal Revenue Code (Code) are to the Code of 1986 as amended to the date of publication.
2. The same general rules also apply for the gift tax deduction under Code Section 2522(c)(2) and Treasury Regulation (Reg.) 25.2522(c)-3(c)(2) (See RR 86-60 *infra*.) For estate taxes, see Code Section 2055(e)(2) and Reg. 20.2055-2(e)(2)(i),(ii),(iii), and (iv).
3. Code Section 170(f)(3)(b).
4. *Id.*
5. See H.R. Report No. 9-413 pt 1 (1969), 1969-3, C.B. 200 237
6. Reg. 1.170A-7(d)(Ex. 3)
7. Code Section 170(f)(3)(B)(i)(ii).
8. Treasury Regulation (Reg.) 1.170A-7(b)(1).
9. *Id.*
10. *Id.*
11. Revenue Ruling 86-60 1986-1 C.B. 302
12. Reg. 1.170A-7(a)(2)(ii)
13. Reg. 1.170A-7(a)(2)(i)
14. Rev. Rul. 77-305, 1977-2 C.B. 72, but see *Blackford Est. v. Comm.*, 77 TC 1246 (1981), *acq.*, 1983-2 C.B. 1, where the remainders under state law could have insisted on the remainder interest rather than the proceeds of sale.
15. Rev. Rul. 75-420, 1975-2 C.B. 78 (Vacation residence qualified)
16. Reg. 1.170A-7(b)(4)
17. PLR 9329017
18. Code Section 170(f)(4)
19. Code Section 170(h)(2)
20. Code Section 170(h)(3)
21. The same general rules also apply for the gift tax deduction under Code Section 2522(c)(2)(A)(B) and Reg. 25.2522(c)-3(c)(2)(v)(vi). For estate taxes, see Reg. 20.2055-2(e)(2)(v)(vi).
22. Code Section 170(f)(2)(A).