



# Is Your Donation Deductible?

## An Orthodox Jew's Guide to the Laws of Charitable Giving - Part One

By Judah I. Kupfer, Esq.

Over the past several months, Agudath Israel of America has initiated the Dina D'Malchusa Dina series of legal seminars project. Responding to the timely need in the Orthodox Jewish community for substantive guidance regarding a range of legal and tax-related issues faced by yeshivos, shuls, gemachs and the general public, Agudath Israel stepped up to fill that need by coordinating this initiative.

To date, Agudath Israel has presented close to ten seminars in various locations across the United States, including programs in Boro Park, Chicago, Cleveland, Flatbush, Lakewood and Los Angeles, and more are scheduled to come. The initiative has been praised by many as long overdue. It has served as a means of educating the greater Orthodox community regarding the intricacies of complicated and often misunderstood legal concepts and has brought about a keen awareness of pertinent rules and laws vital to ensure that organizations and individuals act in compliance with state and federal law. The deductibility of charitable contributions from income tax is one such topic. Below is an article that seeks to clarify the rules of charitable contributions and many of its applications and nuances.

### INTRODUCTION

A feeling of satisfaction accompanies charitable giving. That feeling is amplified when it comes with actual savings in the form of a tax deduction. Last year, charitable giving in the United States was estimated to be in excess of \$300 billion and it is safe to say that the deductibility of charitable contributions has played a key role in increasing the amount people give. By allowing a tax deduction for charitable contributions, the government indirectly subsidizes private philanthropy. While some critics have argued against the idea of the government providing such a subsidy, many people regard activities of charities as socially desirable and appreciate this tax incentive.

It is important to note, however, that not just anything given to further a charitable purpose qualifies for a tax deduction. Congress along with the courts and the Internal Revenue Service have articulated rules regarding which contributions will be deductible. What follows is a synopsis of the elements required for a deductible charitable contribution and some

common applications to Orthodox Jews in the context of schools, *shuls*, *kollelim*, *gemachs* and other charitable organizations. Next week, Part Two will follow with additional illustrations of these principles.

As many of the illustrations are very fact-specific and can change with variations of the smallest details, the reader is cautioned to seek out professional tax advice in connection with his or her specific circumstances, to ensure the proper application of these rules and to be apprised of the many additional rules and nuances that didn't make it into this article.

### Do you need the deduction?

Much value is placed on whether one can deduct a charitable contribution. Often, though, a donor won't end up utilizing that deduction. When calculating taxable income, while certain deductions are available to all, others are limited to taxpayers who elect to itemize their deductions instead of taking the standard deduction. The taxpayer generally chooses whichever method saves him more. The charitable contribution deduction is an example of an itemized deduction (also referred to as a "below-the-line" deduction). For 2010, the taxpayer's itemized expenses for the year need to exceed \$11,400 on joint returns (\$5,700 for single persons) for it to be worthwhile to itemize. Last year, it is estimated that nearly 70% of all taxpayers in the U.S. elected the standard deduction instead of itemizing. Thus, one is encouraged to review past tax returns to gain perspective and consider whether a deduction will be useful.

### What constitutes a deductible charitable contribution?

At the outset, it is important to recognize certain key elements that are required for a contribution to be deductible. First, the donor must make the donation with "donative intent." As it sounds, the donor must intend to make a donation.

Second, the donor may neither receive a benefit in return for his donation nor may he even expect to receive one. The courts have said that donations must be made with "detached and disinterested generosity" - meaning, a donation may not be given in exchange for a past benefit nor with the expectation of a future benefit. To the extent that the donor does in fact receive a benefit in return for his donation, the value of the benefit may not be deducted. (There are exceptions for religious and incidental benefits which will be explained below.) Thus, if the value of the benefit received is equivalent to the donation, the donor may not deduct that donation at all.

Third, a deductible donation is one that is given to a "qualified charitable organization." Most *shuls* and 501(c)(3) organizations are considered qualified charitable organizations. Through this requirement, Congress has consciously decided to exclude donations made to individuals, no matter how worthy the individual's situation may be. Additionally, a qualified charitable organization must be a domestic U.S. organization, i.e., an organization organized under the laws of the United States. With some

limited exceptions to donations made to organizations recognized under the laws of Israel, Canada and Mexico, foreign organizations do not qualify. The details of donating directly to foreign organizations in those countries will not be explored in this article, and may be subject to further restrictions, so please consult a tax advisor if you wish to make such donations.

Donations that do not fit these requirements may be made - but they do not qualify for a tax deduction. In such cases, the donor may not deduct them on his federal tax return and the donee may not issue a receipt. Should the donor nonetheless request a receipt, any receipt provided should be clearly marked as "not tax deductible." If an organization decides to issue a tax-deductible receipt for a donation it knows not to be deductible (and makes no such notation), the organization exposes itself to serious civil and criminal sanctions.

### What are some examples of deductible and non-deductible contributions?

Deductible donations in a *shul* setting include donations to cover the costs for general *shul* expenses (such as the sponsorship of *ner lama'or*, which covers electricity costs). As donors have the option to donate cash or property, a sponsorship of *shul* furniture can consist of writing a check to the *shul* and the *shul* making the purchase. Alternatively, the donor may purchase the furniture directly from the store. In such an instance, the donation would consist of property, i.e., the furniture, and as with any donation of property, the receipt issued to the donor should not assess a value, but rather merely acknowledge receipt of and describe the donated property. The donor would substantiate his deduction through a combination of the *shul* receipt, showing a description of the donated property, and his store receipt, showing the value of the donated property. (The requirements for donating property are complex and the reader is urged to see IRS Publication 526 for additional information.) The merits of donating certain types of property will be discussed below.

Some common examples of non-deductible payments include tuition payments (even for the portion allocated exclusively to religious studies), value of time or services, a "mandatory contribution," and a deposit, i.e., money that the donor expects to get back and/or actually gets back.

If an employer decides to pay the tuition for a child of its employee, absent payments made as part of a Qualified Tuition Reduction Plan (under Internal Revenue Code §117(d)), such payments would ordinarily be considered taxable compensation to the employee. The employer, thus, may not deduct such payments as a charitable contribution, since the employer thereby receives a benefit in exchange for its donation - i.e., the work of the employee (but a business expense deduction for such payments may be available).

### Are there any benefits to donating property?

Certain types of property carry an add-

ed tax advantage when donating the property directly to the organization instead of selling it first and thereafter donating the proceeds. For example, let's say a person purchases publicly traded corporate stock for \$5,000 which grows in value to \$25,000. If the owner were to sell the stock and then turn around and contribute the proceeds, he would realize a taxable gain of \$20,000. By donating the stock as is, assuming he had owned the stock for more than a year, the donor may obtain a tax deduction for the full \$25,000 and need not pay tax on any of the gain in value. Note that contributions of this sort are limited to 30% of the taxpayer's adjusted gross income for the year, to be discussed in more detail in Part Two.

### Is the value of volunteer work deductible?

The value of time or services is not deductible. Thus, the value of volunteer work is not deductible even when provided to help a qualified charitable organization. Some out-of-pocket expenses that the volunteer spends may be deductible - those that are: unreimbursed, directly connected with the services, expenses the donor accumulated only because of the services he provided, and expenses that are not personal living or family expenses. But the donor may not deduct the cost for child-care or any lost income due to volunteering. (The volunteer would be required to substantiate the unreimbursed expenses by obtaining a receipt from the organization acknowledging the volunteer service and whether any goods or services were provided to the volunteer in exchange.)

### May payments made to a school ever be deductible?

While tuition payments are not deductible, payments made to a school separate from tuition, such as a building fund donation, may be deductible under certain circumstances. First, the donation must be made completely voluntarily. The IRS considers various factors to determine the voluntariness of a contribution, including whether the child would have been denied admission to the school had the contribution not been made, whether the enrollment materials imply the contribution to be required, whether the solicitation was made as part of the enrollment process, and whether the parents were under a contractual obligation to make the donation. Additionally, if the donor seeking the deduction is the parent of a student, for such a donation to be deductible it must be clear that the amount of tuition being charged by the school was adequate to support the costs of the child's education. (For donors who do not have children attending the school, the adequacy of tuition rates would not be relevant.) Clearly, calling tuition by another name will not transform non-deductible tuition payments into a deductible donation. Payments made to schools will be scrutinized to determine whether they were in fact non-deductible tuition payments in disguise.

To illustrate, let's assume a school claims not to charge tuition but instead requires a "voluntary" contribution from parents to cover the costs of the educa-

tion. Whether stated explicitly or implicitly, if the policy is such that those who fail to make the "voluntary" contribution are denied admission to the school, the contribution will be deemed not to be a contribution at all but rather non-deductible tuition. Alternatively, should a school require, for example, \$6,000 as tuition and request a \$1,500 voluntary building fund contribution - assuming the \$1,500 is indeed voluntary - such payment would likely be deductible. However, as the IRS considers contributions requested as part of the enrollment process a negative factor in determining voluntariness, the better practice is to conduct the building fund drive at a different time of the year and not as part of the enrollment process so not to give the impression that such funds were part of non-deductible tuition. For additional information on this issue, please refer to IRS Revenue Ruling 83-104 which provides many useful examples of both deductible and non-deductible contributions in the school context.

On the topic of tuition payments, the practice of two sets of parents agreeing that each will pay the other's child's tuition so that each may receive a tax deduction does not work. Such payments to the school are not being made with "detached and disinterested generosity," but are rather part of a scheme to disguise tuition payments as deductible donations. Additionally, as will be explored in Part Two, this scenario raises issues associated with designating a contribution for a specific purpose or individual.

### **What if a donor receives a benefit in exchange for his donation?**

When a benefit is provided in exchange for a donation (known as a "quid pro quo" contribution), the fair market value of the benefit received may not be deducted. Take, for example, one who attends a *yeshiva* dinner. Assuming the dinner fee was \$180 and the fair market value of the dinner was estimated at \$50, the donor may deduct \$130. (Please note: the fair market value of the benefit is not deductible, no matter the cost of the benefit to the donee.) In such an instance (and in any instance where a donor contributes \$75 or more and a benefit of any kind is provided in exchange), the *yeshiva* is required to provide a receipt which assesses an estimated value for the dinner and a notice alerting the donor that the value of the dinner may not be deducted.

Whereas the general obligation to substantiate donations is on the taxpayer, in a scenario where a benefit is provided in exchange for a donation of \$75 or more, the donee organization has an affirmative obligation to issue a receipt in accordance with the above requirements. In our case, sample language can read, "The estimated value of the goods or services received is \$50. Only the amount of your contribution in excess of \$50 is tax deductible."

In the above example, should the donor respond that he will not be attending the dinner but nonetheless encloses a donation of \$180, the full \$180 may be deducted. If instead, the donor initially responded affirmatively to the dinner invitation and then decides not to attend (or if he attends and does not eat), the value of the dinner remains non-deductible. To be deductible in this case, the donor must take affirmative steps before the dinner to reject the benefit by indicating to the *yeshiva* his intention not to attend.

One additional point to mention about

dinners: Even if the entire dinner were to be sponsored by an individual, each attendee must nonetheless subtract the fair market value of the dinner portion received, since the issue is not the cost to the organization but the benefit to the donor. The sponsor of the dinner should obtain a tax deduction for his donation with the exception of his benefit (i.e., the fair market value of his dinner portion).

### **What is an incidental benefit?**

The entire amount of the donation may be deducted when the only benefit provided in exchange is incidental. An incidental benefit is something of "token value," which is estimated currently to be valued at no more than \$9.60 (this number changes over time as it is adjusted for inflation) when the donor makes a minimum donation of \$48. This typically takes the form of a coffee mug or key chain with the charity's logo. Alternatively, if the benefit received is equal to or less than 2% of the donation, the entire donation may be deductible so long as the benefit does not exceed \$96 (adjusted yearly for inflation).

### **What is an intangible religious benefit?**

An intangible religious benefit is defined as "any intangible religious benefit which is provided by an organization organized exclusively for religious purposes and which generally is not sold in a commercial transaction outside the donative context." Examples of such benefits include the cost for purchasing *shul* seats and dues, the purchase of an *aliyah* and the sponsorship of a *parsha* in a new *Sefer Torah*. More questionable cases include whether the money paid to use a *mikvah* may be deducted and whether the cost for purchasing a *lulav* and *esrog* directly from a *shul* may be deducted (on the one hand, the benefit received is religious, yet commercial vendors sell these items).

Examples where the amount paid will likely not be deductible include payments made to a *shul* to purchase wine and *matzoh* for *Pesach* (as these are ordinary consumer goods sold outside the donative context) and the rental cost for a *shul* hall (as the donor receives an ordinary benefit in exchange) unless the cost charged to rent the hall is exaggerated beyond market price. In such an instance, the amount paid beyond market price may be deductible if the donor made the payment with the intent of making a donation. (On that note, the organization should consult with a tax professional to determine if it is required to pay unrelated business income tax on the rental proceeds.)

At the present time, it is well settled that tuition payments made for religious education do not qualify for a charitable deduction, even though the benefit received in exchange can conceivably be seen as an intangible religious benefit.

### **What are the substantiation requirements?**

In order to deduct any contribution, at the time of filing his tax return, the donor/taxpayer must be able to "substantiate" his contribution. The substantiation requirements differ based on the amount and the form of the donation. For cash contributions, a receipt is always needed regardless of the amounts. For a donation in the form of a check of under \$250, a canceled check or bank record showing the amount of the donation and the organization name would suffice. For amounts

of \$250 or more, a receipt is needed.

The receipt must be a written acknowledgment of the donation that includes the amount of cash or description of non-cash property donated, the date of the contribution, the name of the recipient organization and whether it has provided any goods or services to the donor. If goods or services have been provided, a description and good faith valuation of such goods or services must be included. If the donor received an intangible religious benefit, the receipt must include a statement that the only benefit received was an intangible religious benefit.

### **Part Two In Next Week's Paper**

Part Two will address issues of designated/targeted donations, limits to deductible amounts, donor advised funds, rabbi's discretionary funds, the deductibility of raffles tickets and state registration requirements for charitable solicitation of funds.

### **Other Resources**

Helpful resources published by the IRS regarding charitable contributions include: IRS Publications 526 (Charitable Contributions), 1771 (Substantiation and Disclosure), 561 (Determining the Value of Donated Property), 4302 (A Charity's Guide to Vehicle Donations), 4303 (A Donor's Guide to Vehicle Donations), and 597 (Information on the United States - Canada Income Tax Treaty).

Other helpful resources published by the IRS regarding tax-exempt issues include: IRS Publications 1828 (Tax Guide for Churches and Religious Organizations), 4221-PC (Compliance Guide for 501(c)(3) Public Charities), 4220 (Applying for 501(c)(3) Tax-Exempt Status), 557 (Tax-Exempt Status for Your Organi-

zation), and 598 (Tax on Unrelated Business Income of Tax Exempt Organizations).

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*Judah I. Kupfer, Esq. is a staff counsel at Agudath Israel of America. He previously practiced as an associate at the law firm of Allen & Overy LLP in New York. Mr. Kupfer is a summa cum laude graduate of Touro College, a magna cum laude graduate of Brooklyn Law School and an LL.M. taxation candidate at New York University School of Law. To contact the author, email [ykupfer@agudathisrael.org](mailto:ykupfer@agudathisrael.org). Questions and comments are welcome.*

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