

Tax and Legal Update for Charities

By Charles M. Watkins

Congress and the IRS have been busy recently, enacting laws and issuing regulations and other guidance of importance to tax-exempt organizations.

Car Donations

In response to abuses in valuing donations of used cars (and boats and airplanes), Congress enacted new limits on the deduction a donor may claim on account of a gift of a used vehicle to a charity. *P.L. 108-357, §884, adding new I.R.C. §170(f)(12)*. Effective for gifts made on or after January 1, 2005, the deduction for vehicles valued in excess of \$500 is limited to the amount actually received by the charity from the sale of the vehicle. The charity must notify the donor of the amount received within 30 days after the sale.

The only exception is when the charity certifies to the donor that it will use the vehicle in its own activities (including donating the vehicle to a needy individual). In that case, the donor may still claim a deduction for the fair market value of the vehicle, provided he or she obtains a “qualified appraisal” of the vehicle, if the claimed value is more than \$5,000.

The IRS is revising Publications 4302 and 4303 at www.irs.gov, which provide general guidance to charities and donors, respectively, about car donations (see *Publications 4302-A and 4303-A*).

Intellectual Property Donations

New rules apply to determine the amount deductible on account of a gift of a patent, copyright, trademark and similar property. In general, the deduction is limited to the taxpayer's cost of acquiring or developing the property. In subsequent years, the donor may deduct additional amounts based on the income received by the donee from the property. *P.L. 108-357 §882, amending I.R.C. §170(e) and §6050L, and adding new I.R.C. §170(m)*.

In connection with the new rules for valuing gifts of vehicles and intellectual property, Congress codified and amended the rules for substantiating gifts to charities. *P.L. 108-357, §883, adding new I.R.C. §170(f)(11)*.

Technology Gifts

The Working Families Tax Relief Act of 2004, *P.L. 108-311, §306*, extended the enhanced deduction in I.R.C. §170(e)(6) for corporate contributions of scientific property or computer technology to schools, colleges and universities. The enhanced deduction is now available for all contributions made through 2005.

Retirement Plan Issues

■ **Section 403(b) plans:** On November 16, 2004, the IRS published long-awaited proposed regulations under I.R.C. §403(b). *69 Fed. Reg. 67075*. The regulations clarify the

importance of the employer maintaining a plan document—apart from any custodial agreement or annuity contract issued by an insurance company or mutual fund custodian—to ensure that the plan satisfies the applicable non-discrimination and other rules in §403(b), §401(a), and ERISA.

■ **Section 401(k) plans:** On December 29, 2004, the IRS published comprehensive final regulations under §401(k). *69 Fed. Reg. 78144*. Among other things, the rules confirm that a §501(c)(3) organization may terminate its §401(k) plan, and permit participants to immediately transfer their account balances to a successor §403(b) plan (or to an IRA). This helps §501(c)(3) organizations that want to take advantage of the more favorable rules that govern §403(b) plans.

■ **Nonqualified deferred compensation plans:** In October 2004, Congress enacted §409A of the Internal Revenue Code, imposing additional conditions on tax-deferred compensation under nonqualified deferred compensation plans, (other than §457(b) plans). On December 21, 2004, the IRS issued Notice 2005-1, explaining how it will implement the new rules. *P.L. 108-357, §885*.

The new rules include restrictions on elections to defer compensation and distributions, and became effective January 1, 2005. In most cases, the rules will also apply to compensation deferred before 2005 because it was not vested at the end of 2004. In all cases, deferred compensation plans or agreements, will need to be amended during 2005, and must be operated in accordance with the new rules pending the amendment.

California Nonprofit Integrity Act of 2004

California recently amended its Supervision of Trustees for Charitable Purposes Act (Govt. Code §12580 *et seq.*). The law imposes new governance and other requirements on California charities, and on non-California charities that do business or hold property “in California.” The Attorney General (“AG”) has announced that he believes the new rules also apply to non-California charities whose sole contact with California is interstate solicitation of contributions.

A memorandum describing the provisions of the new law and how they will affect charities that are registered or are required to register with the AG's office is available at the CMA Management Resource Center (go to www.CMAonline.org/mrc and click on Tax & Legal Trends and then on Articles and look for “Calif. Nonprofit Integrity Act of 2004”).

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