

Deduction of Charitable Contributions When Benefits Are Received

EACH YEAR TAXPAYERS MAKE CASH CONTRIBUTIONS to a variety of charitable organizations. Sometimes questions arise about whether the contributions are deductible for federal income tax purposes and in what amount, especially if benefits have been received as a result of making a donation. For example: May the cost of the tickets to a charity's annual fundraising event be deducted? How much of a contribution to a university that gives the donor the right to buy tickets to its athletic events is deductible? Is the cost of a membership to a charitable organization deductible?

How much can be deducted if the donor receives a benefit with a value greater than the amount donated in exchange for the donation?

Internal Revenue Code (IRC) §170(c) defines a charitable contribution as a donation or gift to, or for the use of, a qualified organization.

Qualified organizations include nonprofit groups that are religious, charitable, educational, scientific, or literary in purpose or that prevent cruelty to children or animals. Generally, the deductible amount of the contribution to such an organization is the amount actually paid. Yet if a contribution generates a benefit for the taxpayer, only the amount by which the contribution exceeds the value of the benefit received is deductible [Treasury Regulation (Reg) §1.170A-1(h)]. So if John pays \$150 for tickets to a church dinner, and the fair market value (FMV) of the dinner is \$60, he must subtract \$60 from the \$150 paid to determine the deductible portion of his contribution (\$150 - \$60 = \$90).

Similarly, if Susan receives tickets to a charity event, such as a ball, in exchange for a donation to the charity, only the difference between the tickets' price and their FMV (assuming the actual price is higher) can be deducted—even if she does not attend the event. Yet if she returns the tickets to the charity for resale, she can deduct the entire contribution. In reality, the return of the ticket is an additional contribution to the charity. In other words, the original contribution is reduced by the FMV of the charity event, but when the ticket to it is

returned to the charity so that it may be sold to the public, there is an additional donation for the FMV of the ticket, i.e., the FMV of the event.

Further, suppose a charity states in its fundraising information that donors who make a minimum donation of \$40 may receive a

year's subscription to a business journal, which has an FMV of \$80, as a "gift" if they request it when making their pledge. A donor who makes a donation of \$80 or less and requests the subscription has a deductible contribution of \$0 since the FMV of the benefit received exceeds the donation.

In the case of a donation to a university, the outcome may not as straightforward. In general, a donation to a university follows the general rule. Yet if a donor is allowed to buy tickets to an athletic event in exchange for the donation, the deduction is limited to 80% of the donation. For example, if Tom contributes \$500 to a university and receives the right to buy tickets to university athletic events,

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he may only deduct \$400, or 80% of his contribution [IRC §170(l)]. Further, if part of the contribution is actually payment for tickets to an athletic event, the cost of the tickets must be subtracted from the donation before applying the 80% rule. So if Tom receives a season ticket to the university's basketball games for his contribution of \$500, and the cost of a season ticket is \$200, the deductible amount of his contribution is \$240 $[(500 - 200) \times .8]$.

Reg §1.170A-13(f)(8) allows two exceptions to the rule requiring the deductible contribution to be reduced for benefits received. First, donors are allowed to disregard certain membership benefits when calculating the value of benefits received in exchange for a donation of \$75 or less. These benefits include any benefits that can be received

frequently during the membership period, such as:

- Free or discounted admission to the organization's facilities or events,
- Free or discounted parking,
- Preferred access to goods or services,
- Discounts on the purchase of goods and services,
- Admission to events that are open only to members of the organization (if the cost per person is estimated to not exceed a token amount as defined in IRC §513(h)(2)), and
- Token items (a small item or benefit of token value as defined in IRC §513(h)(2)).

To illustrate, Mary's \$65 membership to the Art Museum allows her free and unlimited admission to the museum for the entire year. In addition, she enjoys other benefits, such as a 10% discount in the museum store and restaurant. Depending on the amount of use she makes of her membership, her benefit could exceed the cost of the membership. Yet under Reg. §1.170A-13(f)(8)(B), the entire cost of her Art Museum membership is deductible.

The second exception relates to the receipt of goods or services of "insubstantial value" in exchange for a donation made during a fundraising campaign. Such items are disregarded in determining the amount of the deduction [Reg. §1.170A-13(f)(8)(A)]. For 2002, an item has insubstantial value if its FMV is not more than 2% of the amount of the donation (up to a maximum value of \$79) or if the donation is at least \$39.50, bears the name or logo of the organization, and costs no more

than \$7.90 (Rev Proc 90-12, 1990-1 CB 471, Rev Proc 2001-59, IRB 2001-52). For example, if Bob makes a donation of \$100 to the public radio station during its annual pledge drive, he can deduct the full \$100 donation if what he receives in exchange has an FMV of \$2 $(\$100 \times .02)$ or less and does not bear the name or logo of the station. If the gift *does* bear the name or logo of the station, it can have an FMV of up to \$7.90. Any "gift" with an FMV above these amounts is not of insubstantial value, and the donation must be reduced by the value of the "gift" to determine the deductible contribution.

In the end, the law is fairly straightforward about how the amount of a deductible charitable contribution is determined. Except for memberships of \$75 or less and donations in exchange for items of "insubstantial value," it is the amount by which the donation exceeds the value of what is received in exchange. ■

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