Gift Planning Now

A Newsletter for Berkeley's Donor Advisors

Summer 2013

Appraisal Flaws Defeat Charitable Deduction

Harvey Evenchik owned 72% of the shares of Chateau Apartments, Inc. The company's only assets were two apartment buildings. In 2004, Evenchik gave all of his shares to Family Housing Resources. Evenchik intended for his gift to be used to create an endowment fund which would assist low- to moderate-income individuals and families in obtaining affordable housing.

Evenchik claimed a charitable deduction of $1,045,289, which represented 72% of the value of the apartments, based on two appraisals attached to his return. The IRS audited his 2006 return, on which Evenchik had carried over a portion of the deduction. The IRS disallowed the deduction, saying that he had not provided a qualified appraisal for the gift.

The Tax Court determined that neither appraisal valued the correct asset. Evenchik had given shares of stock, not the underlying assets of the company. In addition, he had given only a fractional interest in the company, but neither appraisal reflected the effect this might have on the value of the shares. Reg. §1.170A-13(c)(3)(ii) requires that the donor provide a description of the gift property sufficient to allow the IRS to determine what was given. Evenchik's appraisals were "woefully short," said the court, noting that the appraisals did not state that they had been prepared for income tax purposes [Reg. §1.170A-13(c)(3)(ii)(G)]. The court rejected Evenchik's argument that he had substantially complied with the regulations, saying that an appraisal of the incorrect assets prevents the IRS from "properly understanding and monitoring the claimed contribution." *Estate of Evenchik v. Commissioner*, T.C. Memo. 2013-34

Sloan Research Fellowships Awarded to Berkeley Faculty

In keeping with tradition, Berkeley faculty continue to be recognized for exceptional work through the receipt of prestigious awards. Of note, two economists, Frederico Finana and Yuriy Gorodnichenko, and two computer scientists, Bjorn Hartmann and Michael Lustig, were recently awarded Sloan Research Fellowships, which are reserved for only the best young scientists in the United States and Canada. These awards highlight the real world application of Berkeley's teaching, research, and public service by Berkeley faculty to better the world around them.

Conveyance Was Quid Pro Quo, Not Charitable Gift

James Pollard wished to build a second home on a parcel of farmland he owned in Colorado, but he needed approval from the county as the lot was slightly smaller than 70 acres. While the county's land use staff recommended that Pollard's request to subdivide be denied, it added that if the recommendation were to be disregarded by the county board, approval should be subject to several conditions. One of these was that Pollard dedicate a conservation easement over the property to the county.

The county eventually agreed to allow the subdivision after Pollard executed a conservation easement that restricted use of the property to two homes and continued use for agriculture. An appraiser, using the before-and-after method, put the value of the easement at $1,049,850, which Pollard claimed on his income tax return. No one from the county signed Pollard's Form 8283. The IRS's appraisal put the value of the easement at $128,000.

A charitable gift for income tax purposes is defined as a payment made "with no expectation of a financial return commensurate with the amount of the gift" [*Hernandez v. Comm'r.*, 490 U.S. 680 (1989)]. The Tax Court noted that the granting of the conservation easement to the county was part of a quid pro quo exchange for the county granting the subdivision request and was of "substantial benefit" to Pollard. The county would not have been inclined to grant Pollard's request had he not granted the conservation easement, said the court. He did not convey the easement for "detached and disinterested motives," but did so to secure a personal benefit. Accordingly, the court ruled that he was not entitled to a charitable contribution deduction. ***Pollard v. Comm'r.*, T.C. Memo. 2013-38**

Tax Planning Pointer

The IRS has approved a two-life charitable remainder unitrust that named a charity as an additional *income* beneficiary. The individual beneficiaries would get at least 25% of the payout, with an independent trustee allocating the remaining 75% between the charity and the individuals (PLR 200813006).

The grantors received no additional deduction for charity's potential payments, but the individual beneficiaries won't be taxed on any charitable distributions. This arrangement may be attractive to donors who want to benefit charity before the trust ends and don't need 100% of the trust payments for their financial security.

Pledge Lesson: Get It In Writing

Before his death, Roland Arnall made three payments of $180,000 to Chabad of California. Chabad claimed that all three gifts were payments on Arnall's $18 million oral pledge. The funds were to be used to construct a new facility.

Following Arnall's death, Chabad sought to enforce the pledge against his estate on the basis of promissory estoppel. Dawn Arnall denied any knowledge of her husband's pledge. The trial court said Chabad failed to prove the existence of the oral promise.

Chabad appealed, saying the trial court erred in refusing to draw negative inferences from Dawn Arnall's alleged withholding of the spreadsheets on which her husband's charitable contributions were recorded by his assistant. According to the assistant, the entries showed the purpose of each entry. Dawn Arnall argued that even without her testimony, there was no affirmative evidence of an oral promise to pay $18 million. The trial court found no evidence that she willfully concealed the spreadsheets.

The California Court of Appeals agreed, saying that the disregard or disbelief of one witness's testimony is not affirmative evidence of a contrary conclusion. Both the trial court and the appellate court noted Chabad's failure to produce any evidence of the oral pledge. ***Chabad of California, Inc. v. Arnall*, B234059**

Receipt Statement Regarding "Goods and Services" Required for Deduction

In 2000, Jolene Villareale founded NDM Ferret Rescue & Sanctuary, which was granted charitable status. As president, she was responsible for the organization's finances, including paying bills and managing its bank accounts.

During 2006, Villareale made 44 contributions to the Sanctuary – 27 for less than $250 (total $2,393) and 17 for $250 or more (total $7,629). The contributions were made electronically or by telephone, transferring funds from her personal account to the Sanctuary's account.

The IRS did not dispute that Villareale made the gifts to the Sanctuary. Rather, it argued that she was not entitled to a deduction for the gifts of $250 or more, because they were not substantiated by contemporaneous written acknowledgments. Villareale claimed that her own bank statements and those of the Sanctuary were sufficient to substantiate the gifts.

The Tax Court agreed with the IRS. Code §170(f)(8)(B)(ii) requires that the contemporaneous written acknowledgments state whether the donor received any goods or services in exchange for the contributions. It is immaterial, said the court, that Villareale was on both sides of the transaction. Although she may not have needed an acknowledgment to help determine the deductible amounts of her gifts, the IRS needed the information to determine whether she was entitled to the deduction claimed. The court added that she did not substantially comply with the substantiation requirements, since the specific statement regarding goods and services "is necessary for the allowance of a charitable deduction." *Villareale v. Comm'r.*, T.C. Memo. 2013-74

Court Holds Lifetime Gifts Did Not Negate Bequests

Charles Walgreen's living trust included bequests of Walgreen stock to numerous charities. During his lifetime he made several gifts to certain of these charities that he characterized as "pre-bequest donations," "prepayment on my bequest" or "advance payment." He had pledged 10,000 shares of Walgreen stock to

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Final Four and a First-Round Draft Pick

Cal Women's Basketball had a historic season! In addition to securing their first-ever Pac-12 title and a berth in the illustrious Final Four, guard Layshia Clarendon '13 became the highest-drafted Golden Bear, when the Indiana Fever selected her as their ninth pick in the first round of the 2013 WNBA Draft.

Court Holds Lifetime Gifts . . . *(continued from page 3)*

Rotary/One Foundation, Inc. and the Rotary Foundation International, both of which were also bequest beneficiaries under his trust. He made outright gifts of 10,000 shares to each foundation in 1999.

At Walgreen's death in 2007, his family claimed that the bequests to the foundations had been adeemed – or satisfied – by the lifetime gifts. The foundations argued that, under Illinois law, the doctrine of ademption did not apply to trusts and that, even if it did, there was no evidence Walgreen intended to adeem these bequests with his lifetime gifts. The trial court granted summary judgment for the foundations. The Appellate Court of Illinois ruled that the doctrine of ademption applies to trusts, noting that courts use the same principles to ascertain a settlor's intent when interpreting a trust document that they do in determining intent in a will. But the court added that written communications between Walgreen and certain charities "unequivocally" showed that when he wished his lifetime gifts to satisfy bequests, he stated as much. Had Walgreen intended to adeem the foundations' bequests with the lifetime gifts, his family would have been able to present the court with supporting evidence. The court declined to presume his intent, which would be "contrary to the plain language of the trust as a whole." *Kouloheorge v. Campbell*, 2012 IL App (1st) 112812

Unsubordinated Mortgage Fatal to Conservation Easement

Walter Minnick claimed a $941,000 deduction for a conservation easement granted in 2006 over a 74-acre parcel in Idaho. At the time of the gift he warranted that there were no outstanding mortgages, although a mortgage had been recorded a year earlier. The IRS initially challenged the valuation of the easement, but later said no deduction was allowable because the mortgage had not been subordinated to the conservation easement. In 2011, at Minnick's request, the lender executed a subordination agreement providing that the easement would remain in effect if the mortgage was foreclosed.

Reg. §1.170A-14(g)(2) provides that no charitable deduction is allowed for a conservation easement over property subject to a mortgage unless the mortgagee subordinates its rights to the charity's rights to enforce the easement. The Tax Court denied Minnick's deduction, saying that any subordination agreement must be in place at the time the conservation easement is granted. Prior to 2011, the lender could have seized the land in the event of a default and would have owned it free of the easement, the court noted. *Minnick and Lienhart v. Commissioner*, T.C. Memo. 2012-345

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