

Donating Non-Publicly Traded Assets to Charity:



Effective and Tax-Efficient Giving During Tough Economic Times.

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During the forty-year period between 1967 and 2007, total charitable giving in the U.S. increased every year but one¹. The lone exception was 1987, a year which was negatively impacted by both a significant late-year stock market decline (20% on a single day in October) and a tax law change that affected allowable deductions. The change prompted some taxpayers to give more in 1986—before the new law was in force—and less in 1987.

The latest uninterrupted growth streak ended in 2008, when total giving declined by 2%—from \$314 million to \$308 million. While this was a modest decline—and positively impressive, considering that the Standard & Poor's 500 Index registered its largest decline in 77 years in 2008, falling 37%—it had a significant impact on charitable organizations, with donations dropping just as need spiked in the communities they serve. Compounding matters, all current reports from the field indicate that the slide in charitable giving has continued in 2009.

It is clear that Americans remain committed to giving in challenging times. But during a recession as deep and indeterminate in length as the current one appears to be, it helps to be creative when creating a personal giving plan. The two types of assets used in individual charitable giving are cash and appreciated publicly traded securities (stocks, bonds, and mutual funds). With public confidence in the economy still shaken, however, more investors are holding on to cash, and are likewise more cautious about donating stock market gains they may have achieved during 2009's mid-year rebound. So donors looking for ways to sustain their charitable giving are increasingly looking for other types of assets to give.

For many, charitable contributions of illiquid assets—private C- and

S-Corp stock, restricted stock, limited partnership interests, and other privately held assets—may be an effective and tax-efficient method of giving. These types of assets, also referred to as non-publicly traded assets, often have a relatively low cost basis (i.e., original cost) for the donor—and in the cases of entrepreneurs who have founded companies, the cost basis may effectively be zero—and a significant current market value which would result in large capital gains taxes if sold. When such an asset is donated to a public charity in the correct and optimal manner, the donor not only avoids the potential capital gains exposure, but is also generally entitled to claim a tax deduction of *the full current market value*² (and not just the original cost basis, as is the case for donations to private foundations). This tax treatment offers significant benefits at the federal level, and frequently at the state and local levels as well.

Contributing non-publicly traded assets to charity, however, can be complicated and is fraught with technical requirements and potential pitfalls. Fortunately, there are organizations that can help guide donors and their advisors through this process, as well as offer valuable planning and technical assistance. One of the largest of these organizations—and one offering several unique advantages—is the Fidelity® Charitable Gift Fund, an IRS-

qualified 501(c)(3) charity with a donor-advised fund program.

Options for Donating Non-Publicly Traded Assets

Once the privately held assets to be donated have been identified (see sidebar on next page for a list of assets in this category), donors and their advisors typically devise a detailed plan outlining immediate and long-term charitable goals, and then consider what would be the best method for donating the assets to realize these goals.

They often quickly find that their options are limited. Many non-profit organizations, being primarily mission- and program-focused, are not well-equipped to handle this type of contribution, and therefore might require that a donor first sell the assets and contribute the proceeds. A donor in this situation would have taxable income and thus would not, in most cases, choose to donate the entire amount of the proceeds, but rather would deduct his/her "cost" to liquidate (including both selling costs and the tax incurred) and then donate the net proceeds—thereby reducing the total amount of the charitable contribution. In this situation, the donor would also only be able to claim a deduction for the amount of the resulting cash contribution, rather than the fair market value of the contributed asset prior to liquidation.

¹ *Giving USA*, a publication of Giving USA Foundation, researched and written by the Center on Philanthropy at Indiana University. Total charitable giving dollars cited are not adjusted for inflation.

² As determined by a qualified appraiser in compliance with IRS rules and regulations.

Further, while some charitable organizations might have some limited experience in handling contributions of non-publicly traded assets, the cost to the charity to outsource the compliance and liquidation work can be considerable. Although the donor would still be eligible to claim a fair market value deduction, the net result to the charity would once again be significantly reduced.

Some donors also consider creating a private foundation, but find even greater complexity, even more obstacles, and higher costs—similarly reducing the amount of money that eventually reaches the donor's chosen charities. Moreover, tax laws allow only the deduction of the *original cost basis* rather than the current market value of most illiquid assets contributed to a private foundation. Donating these types of assets to private foundations is further complicated by IRS rules and regulations related to "self-dealing," "jeopardizing investments" and "excess business holdings." Finally, private foundations must meet a minimum distribution requirement each year; this could present a problem if the foundation's assets are comprised solely or largely of illiquid assets.

In many cases, an optimal method for donating non-publicly traded assets to charity—measured by cost, flexibility, simplicity, and tax benefits to the donor, as well as by maximizing the net proceeds ultimately made available to charitable organizations—is to make the contribution to a charity that offers donor-advised funds. Most of the larger donor-advised fund programs in the U.S., including the Fidelity® Charitable Gift Fund, have the requisite expertise and dedicated professional resources to work with donors and their advisors directly to maximize the giving power of these assets. Most acceptance decisions can be made within a few days once the necessary information is received.

How a Donor-Advised Fund Works

For those who may not be familiar with the concept, some public charities

have donor-advised fund (or "DAF") programs. In a donor-advised fund program, donors make irrevocable contributions of cash or securities to the charity, and the charity then establishes an account from which the donor is able to recommend grants to other eligible charities—generally speaking, IRS-qualified 501(c)(3) public charities—from the balance in their DAF account.

The benefits of the donor-advised fund are numerous. First, donors are able to make a charitable contribution and are eligible for a tax deduction on that contribution, in a specific year, while spacing out their grants over a period of years³. Donors are permitted, of course, to make further contributions at any time, but having the balance in place in their DAF means that they can engage in longer-term charitable giving, allowing them to maintain a certain level of giving regardless of changing financial circumstances—a critical point for both donors and their recommended charities during challenging economic times.

Second, individuals who create a donor-advised fund are typically also able to recommend how those funds should be *invested*. Many DAFs offer a variety of investment pools that allow donors to recommend the investment style that fits best with their time horizon for recommending charitable grants—Growth, Fixed Income, Money Market, or blended investments. The funds that have been contributed to the DAF have the opportunity thereafter to grow tax-free⁴. In addition, DAF programs provide consolidated tax reporting for the year's contributions, eliminating paperwork for the donor and simplifying and improving compliance with IRS requirements.

Donor-advised funds are simple, flexible and cost-effective. They help donors achieve strategic, thoughtful giving for themselves and in many cases for their entire family. Often, in fact, donor-advised funds are established in the name of a donor's family; by planning for charitable contribu-

Types of Non-Publicly Traded Assets That Can Be Donated to Charity

- Private Company Stock
 - S-Corp
 - C-Corp
- Restricted Stock
- LLC and Limited Partnership Interests
- Real Estate
- Pre-IPO Shares
- Personal property (artwork, collectibles⁵)
- Other miscellaneous capital assets

tions and grants over a period of time—one year, five years, ten years or more—families can make a continuing difference.

Donating Non-Publicly Traded Assets via a Donor-Advised Fund

In the specific case of donating non-publicly traded assets, the sponsoring charity of the DAF, as the legal owner of the assets, once contributed, has the responsibility for liquidating the non-publicly traded assets in compliance with IRS rules and regulations—including handling all legal review of documents and IRS reporting. This enables the grant-receiving charitable organizations to focus on what they do best—fulfilling the organization's charitable mission—rather than overseeing an often-complicated financial and legal process and being responsible for "getting it right" both for the donor and for themselves. Also, and as mentioned, the donation of these assets to a charity with a donor-advised fund program—and the subsequent liquidation by the sponsoring charity—means that

³ Subject to program's grantmaking policies.

⁴ Of course, investing also involves risk, including risk of loss to the charity and the individual Giving Account®.

⁵ Related use needed to claim a fair market tax deduction.

donors themselves realize no capital gain, and thus pay no capital gains tax⁶. This helps ensure that the highest possible percentage of the funds from the sale of the asset or assets actually goes to the chosen charitable organizations.

Perhaps best of all, by donating non-publicly traded assets to establish a DAF, these donors are able to *diversify their giving with one asset* in that they are able to recommend multiple grants to many different charities, as opposed to donating the asset (or assets) to one non-profit organization—or going through a transfer agent to break up the asset to facilitate multiple gifts. The experienced charitable giving professionals at the DAF program are able to do this work for the donor.

The Fidelity® Charitable Gift Fund and Its Mission

The Fidelity® Charitable Gift Fund (“Gift Fund”) is the nation’s largest donor-advised fund program and third largest independent public charity⁷. Fidelity Charitable Services®, a leading provider of charitable solutions for individuals, advisors and companies, provides administrative services to the Gift Fund.

The Gift Fund’s mission is to further the American tradition of philanthropy by providing programs that make charitable giving simple and effective. Among DAF providers, the Gift Fund has one of the lowest annual fees (currently 0.6 percent) and one of the lowest minimum initial contribution requirements (currently \$5,000, though it can be higher for non-publicly traded asset donations). The Gift Fund does not charge a direct fee⁸ for helping its donors contribute non-publicly traded assets (only unrelated business income tax, if applicable, actual carrying and maintenance costs, and certain tax preparation consultancy costs are taken from the proceeds of the sale of the contributed asset). Quite apart from

fees, however, the Fidelity® Charitable Gift Fund offers a level of expertise in this area matched by few organizations in the U.S.

The Gift Fund’s goal is to make charitable giving as easy and painless as possible, both for the donor and for the donor’s lawyers and/or advisors. This is especially relevant in connection with contributions of complex assets—and, according to our donors and their advisors, we are succeeding at this goal.

What Gift Fund Donors and their Advisors Say

One of these advisors is Joseph Crocker, CFP®, CIMA and Managing Director of Chess Financial Corporation, who worked with the Gift Fund to help accept a donation of private S-Corp stock on behalf of his entrepreneur client in 2008. According to Crocker, “This was my and Chess’ first foray into this type of transaction and, working with the Gift Fund, it was a smooth process from beginning to end—smooth, above all, because of the Gift Fund’s follow-through at every step of the way. Nothing fell through the cracks. The knowledge and experience the Gift Fund brought to the table helped turn a transaction that I think can be a nine or a ten, in terms of difficulty, into about a three.”

Steven C. Mayer, a Gift Fund donor, is the chief executive officer and co-founder of CoGenesys, a biotechnology company located in Maryland. In his words, as he prepared to sell his interest in the privately held company in 2007, “I wanted to create an ongoing charitable concern, something to serve as a legacy for me and my whole family. I thought first of establishing a private foundation, but found there were two problems: one, that donating privately held stock to a private foundation is not a tax-efficient option, and two, that the administrative challenges were considerable and expensive. Establish-

ing a DAF at the Fidelity® Charitable Gift Fund was absolutely the best option. Throughout the donation process, which went very smoothly, and afterwards as the Gift Fund worked with the company to liquidate its shares in the corporate transaction, the Gift Fund distinguished itself as a top-tier organization. I look forward to a long association.”

Conclusion

When it comes to helping donors and their advisors donate non-publicly traded assets to charity, the Fidelity® Charitable Gift Fund is an ideal option, offering the knowledge and experience to get the job done correctly, promptly, and with all appropriate follow-through, as well as the scale to be able to offer this individual assistance at no cost to donors or to their advisors or legal counsel (apart from actual, “pass-through” costs). If you have questions about non-publicly traded asset donations, please call [800.682.4438](tel:800.682.4438) to talk with a Charitable Planning Associate today or visit our web site at CharitableGift.org/special-assets.

Continuing to grow charitable giving during tough economic times is a challenge—for both philanthropically-minded Americans and for non-profit organizations trying to raise the necessary funds to achieve their mission. But it’s worth noting that even through the extraordinarily difficult financial climate of 2008 and into 2009, the number of donors to the Gift Fund continues to rise. And throughout our history, Americans have always shown, in good times and bad, that where there is a will, there is a way. ■

⁶ Assumes that the donor does not have an anticipatory assignment of income issue.

⁷ Source: The Philanthropy 400, The Chronicle of Philanthropy, October 30, 2008 (based on contributions from individuals, foundations, and corporations).

⁸ The Gift Fund charges administrative and investment management fees.

The Fidelity® Charitable Gift Fund (“Gift Fund”) is an independent public charity with a donor advised fund program. Various Fidelity companies provide investment management and administrative services to the Gift Fund. The Charitable Gift Fund logo is a service mark of the Trustees of the Fidelity Investments® Charitable Gift Fund. Fidelity and Fidelity Investments are registered service marks of FMR LLC, used by the Gift Fund under license. 522156.2.0