Should Your Organization Accept that Gift?

By Ted R. Batson, Jr., Partner

We've all heard the adage "Never look a gift horse in the mouth," but that is not sound advice for nonprofits. Not all gifts are equal, and not all gifts are free. In fact, some gifts may have implications or costs that could have negative consequences for your organization.

In a previous article, we explained how to create a gift acceptance policy that ensures your organization considers the potential impact of a gift, and provides your donors and staff with clear guidelines on your organization's policies for accepting gifts. Now we'll examine specific issues around gift restrictions, gifts with associated costs, gift agreements, and other considerations.

Restrictions and Conditions on Gifts

Donors frequently wish to provide a gift to fund a specific project or program. A core principle in charitable giving is that the recipient organization must take exclusive ownership and control over each gift and exercise control and discretion over the use of the gift. Within this context, it is permissible for a charitable organization to accept a contribution subject to a donor's express or implied intent as to the use of the gift so long as the purpose of the gift is consistent with the organization's exempt purpose.

While a restriction may be permissible, it may leave an organization with unusable funds if the purpose of the restriction becomes impossible or infeasible in the future. For example, a gift intended to endow a fund for maintenance of a specific building will be frustrated if the building is sold, torn down, or otherwise becomes unavailable. While an organization may go back to a donor and request that the restriction be lifted, this may be impossible if the donor passes away or becomes incapacitated. Where the donor is not available to lift a restriction, an organization may petition a court to alter the restriction; however, such an action requires significant additional expense.

To avoid the undesirable consequences of a donor restriction, it is strongly recommended that you encourage donors to impose the least restrictive restriction possible. To document the donor's intent, it is customary to incorporate the understanding in a written gift agreement. In addition to limiting the scope of a restriction, it is also desirable to include a power permitting the exempt organization to alter the restriction (a so-called variance power) when the purpose of the restriction becomes impossible or impracticable.

A condition on a gift may be a restriction on the use of the gift after the transfer or may impose a requirement before the exempt organization can use the asset. For example, the donor may require that the organization delay the sale of stock for some period after contribution. A pre-condition on use will generally mean the gift is incomplete until the condition is met or otherwise removed. The donor will not be able to claim an income tax deduction for the gift until any condition is removed.

Not All Gifts Are Free

Not all gifts are as simple as receiving a check or a transfer of publicly traded securities. In some cases, your organization may need to obtain legal counsel to review circumstances surrounding the receipt of a gift. For example, if your organization is offered stock in a closely-held corporation, you may be asked to agree to sign a shareholders' agreement that prescribes conditions on your ownership of the stock (e.g., you may be limited to selling the stock to other shareholders). Moreover, if that same stock is the subject of a sale, you may be presented with a purchase agreement to sign. In either case, you should engage legal counsel to review these agreements before signing.

In addition to legal fees, receipt of a gift may require transportation of the gift from the donor to your organization or some other cost of delivery. The donor may be willing to supplement the gift with cash to cover these additional costs, in whole or in part. Regardless, the existence of these costs remains a real consideration.

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The donor may also require an appraisal to substantiate the value of his or her contribution for income tax purposes. Donors frequently request that the recipient of their gift pay the fee for the preparation of the appraisal report. As a best practice, your organization should *not* pay for the donor's appraisal. This could be a private benefit and, if the donor is a disqualified person, it could be an excess benefit transaction that would subject your organization and the donor to excise taxes. However, if your organization elects to pay the appraisal fee, your letter acknowledging the gift should clearly disclose the amount of the fee as quid pro quo paid in exchange for the gift.

Gift Agreements

For gifts of noncash assets, assets that involve additional costs, or gifts that involve a donor restriction, it is a best practice to create a written gift agreement that captures the mutual understanding and agreement of the exempt organization and the donor. The topics frequently covered in a gift agreement include:

- The nature of the asset contributed;
- The existence of any restrictions and the conditions on which the restriction may be amended or removed;
- Which party is responsible for any costs; and
- Any donor recognition to be given.

A Few Words About Specific Types of Gifts

Not all gifts are created equal. Some gifts require special care in accepting the gift, planning for care after the gift, or both.

Real property. Real property gifts can provide significant benefit. However, your organization should consider several points prior to accepting a real property gift:

- The property should be examined for environmental contamination
- To protect your organization's title to the property, you should consider obtaining a title insurance policy
- For buildings and other structures, you should obtain insurance covering the structure
- For vacant buildings and similar property, you should arrange for security for the building
- For property that may have a crop or other perishable element, provision should be made for harvesting or otherwise preserving the property

Closely-held business interests. Closely-held business interests may also be a source of significant gifts. However, closely-held business interests can also pose unique challenges. For example, a contribution of S-corporation stock will produce unrelated business taxable income to the extent the business produces net income from any source during the period the exempt organization is the owner. Further, a limited liability company interest, limited partnership interest, general partnership interest, or other passthrough entity interest may produce unrelated business taxable income during the year.

Works of Art and Other Collectibles. Works of art and collectibles (e.g., a stamp collection, coin collection, gun collection, or pottery collection) require special care:

- Proper transportation and delivery of the art or collection must be arranged
- The art or collection should be insured against loss
- Proper storage should be arranged, which in some cases may involve a specialized storage facility with environmental controls governing temperature and humidity

Conclusion

Carefully considering and planning for the issues outlined above will help your organization accept gifts in a way that provides maximum benefit. We can assist you in assessing specific gifts or types of gifts and the potential implications for your organization. Please contact us for details.

About the Author

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As a certified public accountant and tax counsel, Ted advises exempt organizations of all sizes on a wide range of issues. This includes consulting on tax and employee benefit related matters, representation before state and federal tax authorities, and assistance with firm audit or advisory engagements to formulate advice and counsel on important operating and tax issues. Ted also leads the firm's tax preparation practice, including IRS Forms 990 and 990-T and related state forms.

Note: Although licensed to practice law in Indiana, Ted's services through CapinCrouse do not involve the practice of law and consequently do not result in the creation of an attorney-client relationship.

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